LANDEC CORP \CA\
Form 10-K
July 27, 2007

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-K

x ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the Fiscal Year Ended May 27, 2007, or

o TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the Transition period for _________ to _________.

Commission file number: **0-27446**

LANDEC CORPORATION
(Exact name of registrant as specified in its charter)

California	**94-3025618**
(State or other jurisdiction of incorporation or organization)	(IRS Employer Identification Number)

3603 Haven Avenue
Menlo Park, California 94025
(Address of principal executive offices)

Registrant's telephone number, including area code:
(650) 306-1650
Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Name of each exchange on which registered
Common Stock	The NASDAQ Stock Market, Inc.

Securities registered pursuant to Section 12(g) of the Act:
None
(Title of Class)

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.
Yes o No x

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act.
Yes o No x

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Act during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes x No o

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. x

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Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of “accelerated filer and large accelerated filer” in Rule 12b-2 of the Act.

Large Accelerated Filer o Accelerated Filer x Non Accelerated Filer o

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act).

Yes o No x

The aggregate market value of voting stock held by non-affiliates of the Registrant was approximately $209,754,000 as of November 26, 2006, the last business day of the registrant’s most recently completed second fiscal quarter, based upon the closing sales price on The NASDAQ Global Select Market reported for such date. Shares of Common Stock held by each officer and director and by each person who owns 10% or more of the outstanding Common Stock have been excluded from such calculation in that such persons may be deemed to be affiliates. This determination of affiliate status is not necessarily a conclusive determination for other purposes.

As of July 13, 2007, there were 25,904,212 shares of Common Stock outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the registrant’s definitive proxy statement relating to its October 2007 Annual Meeting of Shareholders, which statement will be filed not later than 120 days after the end of the fiscal year covered by this report, are incorporated by reference in Part III hereof.

LANDEC CORPORATION
ANNUAL REPORT ON FORM 10-K

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PART I

Item 1. *Business*

This report contains forward-looking statements within the meaning of Section 21E of the Securities Exchange Act of 1934. Words such as “projected,” “expects,” “believes,” “intends” and “assumes” and similar expressions are used to ident forward-looking statements. These statements are made based upon current expectations and projections about our business and assumptions made by our management and are not guarantees of future performance, nor do we assume any obligation to update such forward-looking statements after the date this report is filed. Our actual results could differ materially from those projected in the forward-looking statements for many reasons, including the risk factors listed in Item 1A. “Risk Factors” and the factors discussed below.

General

Landec Corporation and its subsidiaries (“Landec” or the “Company”) design, develop, manufacture and sell temperature-activated and other specialty polymer products for a variety of food products, agricultural products, and licensed partner applications. The Company’s proprietary polymer technology is the foundation, and a key differentiating advantage, upon which Landec has built its business.

The principal products and services offered by the Company in its two historical core businesses - Food Products Technology and Agricultural Seed Technology - and in the Technology Licensing/Research and Development business are described below. Financial information concerning the industry segments for which the Company reported its operations during fiscal years 2005, 2006 and 2007 is summarized in Note 15 to the Consolidated Financial Statements.

Landec’s Food Products Technology business, operated through its subsidiary Apio, Inc., combines Landec’s proprietary food packaging technology with the capabilities of a large national food supplier and value-added produce processor. This combination was consummated in 1999 when the Company acquired Apio, Inc. and certain related entities (collectively “Apio”).

Landec’s Agricultural Seed Technology business is operated through a subsidiary, Landec Ag, Inc. (“Landec Ag”) which, prior to the sale of Fielder’s Choice Direct (“FCD”) on December 1, 2006 to American Seeds, Inc. (ASI), a wholly owned subsidiary of Monsanto Company (“Monsanto”), (see Note 2 to the Consolidated Financial Statements), combined the Company’s proprietary Intellicoat® seed coating technology with FCD’s unique direct marketing and sales capabilities.

In addition to its two historical core businesses, the Company also operates a Technology Licensing business that licenses products to, and conducts joint research and development with industry leaders outside of Landec’s core businesses, such as Air Products and Chemicals, Inc. (“Air Products”). The Company also engages in research and development activities and supplies products based on its Intelimer® polymer technology to companies such as Akzo-Nobel Chemicals B.V. (“Akzo-Nobel”) and L’Oreal of Paris (“L’Oreal”) (these supply activities are included in the technology fields licensed to Air Products). For segment disclosure purposes, the Technology Licensing business is included in Corporate and Other in Note 15 to the Consolidated Financial Statements.

The Company's core polymer products are based on its patented proprietary Intelimer polymers, which differ from other polymers in that they can be customized to abruptly change their physical characteristics when heated or cooled through a pre-set temperature switch. For instance, Intelimer polymers can change within the range of one or two degrees Celsius from a non-adhesive state to a highly tacky, adhesive state; from an impermeable state to a highly permeable state; or from a solid state to a viscous liquid state. These abrupt changes are repeatedly reversible and can

be tailored by Landec to occur at specific temperatures, thereby offering substantial competitive advantages in the Company's target markets.

The Company was incorporated in California on October 31, 1986. The Company completed its initial public offering in 1996 and is listed on The NASDAQ Global Select Market under the symbol “LNDC”.

Technology Overview

Polymers are important and versatile materials found in many of the products of modern life. Certain polymers, such as cellulose and natural rubber, occur in nature. Man-made polymers include nylon fibers used in carpeting and clothing, coatings used in paints and finishes, plastics such as polyethylene, and elastomers used in automobile tires and latex gloves. Historically, synthetic polymers have been designed and developed primarily for improved mechanical and thermal properties, such as strength and the ability to withstand high temperatures. Improvements in these and other properties and the ease of manufacturing of synthetic polymers have allowed these materials to replace wood, metal and natural fibers in many applications over the last 50 years. More recently, scientists have focused their efforts on identifying and developing sophisticated polymers with novel properties for a variety of commercial applications.

Landec's Intelimer polymers are a proprietary class of synthetic polymeric materials that respond to temperature changes in a controllable, predictable way. Typically, polymers gradually change in adhesion, permeability and viscosity over broad temperature ranges. Landec's Intelimer materials, in contrast, can be designed to exhibit abrupt changes in permeability, adhesion and/or viscosity over temperature ranges as narrow as 1°C to 2°C. These changes can be designed to occur at relatively low temperatures (0°C to 100°C) that are relatively easy to maintain in industrial and commercial environments. *Figure 1* illustrates the effect of temperature on Intelimer materials as compared to typical polymers.

Landec's proprietary polymer technology is based on the structure and phase behavior of Intelimer materials. The abrupt thermal transitions of specific Intelimer materials are achieved through the controlled use of hydrocarbon side chains that are attached to a polymer backbone. Below a pre-determined switch temperature, the polymer's side chains align through weak hydrophobic interactions resulting in a crystalline structure. When this side chain crystallizable polymer is heated to, or above, this switch temperature, these interactions are disrupted and the polymer is transformed into an amorphous, viscous state. Because this transformation involves a physical and not a chemical change, this process is repeatedly reversible. Landec can set the polymer switch temperature anywhere between 0°C to 100°C by varying the length of the side chains. The reversible transitions between crystalline and amorphous states are illustrated in *Figure 2* below.

Side chain crystallizable polymers were first discovered by academic researchers in the mid-1950's. These polymers were initially considered to be merely of scientific curiosity from a polymer physics perspective, and, to the Company's knowledge, no significant commercial applications were pursued. In the mid-1980's, Dr. Ray Stewart, the Company's founder, became interested in the idea of using the temperature-activated permeability properties of these polymers to deliver various materials such as drugs and pesticides. After forming Landec in 1986, Dr. Stewart subsequently discovered broader utility for these polymers. After several years of basic research, commercial development efforts began in the early 1990's, resulting in initial products in mid-1994.

Landec's Intelimer materials are generally synthesized from long side-chain acrylic monomers that are derived primarily from natural materials such as coconut and palm oils that are highly purified and designed to be manufactured economically through known synthetic processes. These acrylic-monomer raw materials are then polymerized by Landec leading to many different side-chain crystallizable polymers whose properties vary depending upon the initial materials and the synthetic process. Intelimer materials can be made into many different forms, including films, coatings, microcapsules and discrete forms.

Description of Core Business

The Company has historically participated in two core business segments- Food Products Technology and Agricultural Seed Technology. In addition to these two core segments, Landec licenses technology and conducts ongoing research and development and supplies materials through its Technology Licensing business.

Food Products Technology Business

The Company began marketing its proprietary Intelimer-based BreatheWay® membranes in 1996 for use in the fresh-cut produce packaging market, one of the fastest growing segments in the produce industry. Landec's proprietary BreatheWay packaging technology when combined with fresh-cut or whole produce results in packaged produce with increased shelf life and reduced shrink (waste) without the need for ice during the distribution cycle. The resulting products are referred to as "value-added" products. In 1999, the Company acquired Apio, its then largest customer in the Food Products Technology business and one of the nation's leading marketers and packers of produce and specialty packaged fresh-cut vegetables. Apio utilizes state-of-the-art fresh-cut produce processing technology and year-round access to specialty packaged produce products which Apio distributes to the top U.S. retail grocery chains, major club stores and to the foodservice industry. The Company's proprietary BreatheWay packaging business has been combined with Apio into a subsidiary that retains the Apio, Inc. name. This vertical integration within the Food Products Technology business gives Landec direct access to the large and growing fresh-cut and whole produce market.

The Technology and Market Opportunity: Proprietary BreatheWay Packaging Technology

Certain types of fresh-cut and whole produce can spoil or discolor rapidly when packaged in conventional packaging materials and are therefore limited in their ability to be distributed broadly to markets. The Company's proprietary BreatheWay packaging technology extends the shelf life and quality of fresh-cut and whole produce.

Fresh-cut produce is pre-washed, cut and packaged in a form that is ready to use by the consumer and is thus typically sold at premium price levels compared to unpackaged produce. The total U.S. fresh produce market is estimated to be between $100 to $120 billion. Of this, U.S. retail sales of fresh-cut produce is estimated to comprise 10% of the fresh produce market. The Company believes that the growth of this market has been driven by consumer demand and the willingness to pay for convenience, freshness, uniform quality, safety and nutritious produce delivered to the point of sale. According to the International Fresh-Cut Produce Association, the fresh-cut produce market is one of the highest growth areas in retail grocery stores.

Although fresh-cut produce companies have had success in the salad market, the industry has been slow to diversify into other fresh-cut vegetables or fruits due primarily to limitations in film and plastic tray materials used to package fresh-cut produce. After harvesting, vegetables and fruit continue to respire, consuming oxygen and releasing carbon dioxide. Too much or too little oxygen can result in premature spoilage and decay and, in some cases, promote the growth of microorganisms that jeopardize inherent food safety. Conventional packaging films used today, such as polyethylene and polypropylene, can be made with modest permeability to oxygen and carbon dioxide, but often do not provide the optimal atmosphere for the produce packaged. Shortcomings of conventional packaging materials have not significantly hindered the growth in the fresh-cut salad market because lettuce, unlike many vegetables and fruit, has low respiration requirements.

The respiration rate of produce varies from vegetable-to-vegetable and from fruit-to-fruit. The challenge facing the industry is to develop packaging for the high respiring, high value and shelf life sensitive vegetable and fruit markets. The Company believes that today's conventional packaging films face numerous challenges in adapting to meet the diversification of pre-cut vegetables and fruit evolving in the industry without compromising shelf life and produce quality. To mirror the growth experienced in the fresh-cut salad market, the markets for high respiring vegetables and fruit such as broccoli, cauliflower, asparagus, papayas, bananas and berries will require a more versatile and sophisticated packaging solution for which the Company's BreatheWay packaging technology was developed.

The respiration rate of produce also varies with temperature. As temperature increases, produce generally respires at a higher rate, which speeds up the aging process, resulting in shortened shelf life and increased potential for decay, spoilage, and loss of texture and dehydration. As produce is transported from the processing plant through the refrigerated distribution chain to foodservice locations, retail grocery stores and club stores, and finally to the ultimate

consumer, temperatures can fluctuate significantly. Therefore, temperature control is a constant challenge in preserving the quality of fresh-cut and whole produce — a challenge few current packaging films can compensate for. The Company believes that its temperature-responsive BreatheWay packaging technology is well suited to the challenges of the produce distribution process.

Using its Intelimer polymer technology, Landec has developed packaging technology that it believes addresses many of the shortcomings of conventional packaging materials. A membrane is applied over a small cutout section or an aperture of a flexible film bag or plastic tray. This highly permeable “window” acts as the mechanism to provide the majority of the gas transmission requirements for the entire package. These membranes are designed to provide three principal benefits:

- *High Permeability.* Landec's BreatheWay packaging technology is designed to permit transmission of oxygen and carbon dioxide at 300 times the rate of conventional packaging films. The Company believes that these higher permeability levels will facilitate the packaging diversity required to market many types of fresh-cut and whole produce.

- *Ability to Adjust Oxygen and Carbon Dioxide Permeability.* BreatheWay packaging can be tailored with carbon dioxide to oxygen transfer ratios ranging from 1.0 to 12.0 and selectively transmit oxygen and carbon dioxide at optimum rates to sustain the quality and shelf life of packaged produce.

- *Temperature Responsiveness.* Landec has developed breathable membranes that can be designed to increase or decrease permeability in response to environmental temperature changes. The Company has developed packaging that responds to higher oxygen requirements at elevated temperatures but is also reversible, and returns to its original state as temperatures decline. The temperature responsiveness of these membranes allows ice to be removed from the distribution system which results in numerous benefits. These benefits include (1) a substantial decrease in freight cost, (2) reduced risk of contaminated produce because ice can be a carrier of micro organisms, (3) the elimination of expensive waxed cartons that cannot be recycled, and (4) the potential decrease in work related accidents due to melted ice.

Landec believes that growth of the overall produce market will be driven by the increasing demand for the convenience of fresh-cut produce. This demand will in turn require packaging that facilitates the quality and shelf life of produce transported to fresh-cut distributors in bulk and pallet quantities. The Company believes that in the future its BreatheWay packaging technology will be useful for packaging a diverse variety of fresh-cut and whole produce products. Potential opportunities for using Landec’s technology outside of the produce market exist in cut flowers and in other food products.

Landec is working with leaders in the club store, retail grocery chain and foodservice markets. The Company believes it will have growth opportunities for the next several years through new customers and products in the United States, expansion of its existing customer relationships, and through export and shipments of specialty packaged produce.

Landec manufactures its BreatheWay packaging through selected qualified contract manufacturers. In addition to using BreatheWay packaging for its value-added produce business, the Company markets and sells BreatheWay packaging directly to food distributors.

The Business: Apio, Inc.

Apio had revenues of approximately $206 million for the fiscal year ended May 27, 2007, $195 million for the fiscal year ended May 28, 2006 and $179 million for the fiscal year ended May 29, 2005.

Based in Guadalupe, California, Apio, when acquired in 1999, consisted of two major businesses - first, the “fee-for-service” selling and marketing of whole produce and second, the specialty packaged fresh-cut and whole value-added processed products that are washed and packaged in our proprietary BreatheWay packaging. The “fee-for-service” business historically included field harvesting and packing, cooling and marketing of vegetables and fruit on a contract basis for growers in California’s Santa Maria, San Joaquin and Imperial Valleys as well as in Arizona and Mexico. The Company exited this business and certain assets associated with the business were sold in

June 2003 to Beachside Produce, LLC. Beachside Produce is owned by a group of entities and persons that supply produce to Apio, including Nicholas Tompkins, Apio's President and Chief Executive Officer. Under the terms of the sale, Beachside Produce purchased certain equipment and carton inventory from Apio in exchange for approximately $410,000. In connection with the sale, Beachside Produce has paid Apio royalty fees per carton sold for the use of Apio's brand names and Beachside Produce and its owner growers entered into a long-term supply agreement with Apio to supply produce to Apio for its fresh-cut value-added business. The fresh-cut value-added processed products business markets a variety of fresh-cut and whole vegetables to the top retail grocery chains, club stores and foodservice suppliers. During the fiscal year ended May 27, 2007, Apio shipped nearly seventeen million cartons of produce to leading supermarket retailers, wholesalers, foodservice suppliers and club stores throughout the United States and internationally, primarily in Asia.

There are five major distinguishing characteristics of Apio that provide competitive advantages in the Food Products Technology market:

- **Value-Added Supplier:** Apio has structured its business as a marketer and seller of fresh-cut and whole value-added produce. It is focused on selling products under its Eat Smart® brand and other brands for its fresh-cut and whole value-added products. As retail grocery and club store chains consolidate, Apio is well positioned as a single source of a broad range of products.

- **Reduced Farming Risks:** Apio reduces its farming risk by not taking ownership of farmland, and instead, contracts with growers for produce. The year-round sourcing of produce is a key component to the fresh-cut and whole value-added processing business.

- **Lower Cost Structure:** Apio has strategically invested in the rapidly growing fresh-cut and whole value-added business. Apio's 96,000 square foot value-added processing plant, which was recently expanded from 60,000 square feet, is automated with state-of-the-art vegetable processing equipment. Virtually all of Apio's value-added products utilize Apio's proprietary BreatheWay packaging technology. Apio's strategy is to operate one large central processing facility in one of California's largest, lowest cost growing regions (Santa Maria Valley) and use packaging technology to allow for the nationwide delivery of fresh produce products.

- **Export Capability:** Apio is uniquely positioned to benefit from the growth in export sales to Asia and Europe over the next decade with its export business, Cal-Ex. Through Cal-Ex, Apio is currently one of the largest U.S. exporters of broccoli to Asia and is selling its iceless products to Asia using proprietary BreatheWay packaging technology.

- **Expanded Product Line Using Technology:** Apio, through the use of its BreatheWay packaging technology, is introducing on average fifteen new value-added products each year. These new product offerings range from various sizes of fresh-cut bagged products, to vegetable trays, to whole produce, to a meal line of products. During fiscal year 2007, Apio introduced 15 new products.

Apio established its Apio Tech division in 2005 to advance the sales of BreatheWay packaging technology for shelf-life sensitive vegetables and fruit, including unique packaging solutions for produce in large packages including shipping and pallet-sized containers.

For the past eleven years, the Company has marketed its Eat Smart fresh-cut bagged vegetables, trays and iceless products using its BreatheWay packaging technology and has now expanded its technology to include packaging for bananas. In September 2004, Apio entered into an agreement with Chiquita Brands International, Inc. ("Chiquita") whereby Apio supplies Chiquita with its proprietary banana packaging technology on a worldwide basis for the ripening, conservation and shelf-life extension of bananas in selective applications on an exclusive basis and for other applications on a non-exclusive basis. In addition, Apio provides Chiquita with ongoing research and development and process technology support for the BreatheWay membranes and bags, and technical service support throughout the customer chain in order to assist in the development and market acceptance of the technology.

For its part, Chiquita provides marketing, distribution and retail sales support for Chiquita bananas sold worldwide in BreatheWay packaging. To maintain the exclusive license, Chiquita must meet annual minimum purchase thresholds of BreatheWay banana packages.

The initial market focus for the BreatheWay banana packaging technology using Chiquita® Brand bananas will be commercial outlets that normally do not sell bananas because of their short shelf-life - outlets such as quick serve restaurants, convenience stores, drug stores and coffee chain outlets. Chiquita has recently started market testing the sale of bananas packaged with Landec's BreatheWay technology to retail grocery chains.

The Company's specialty packaging for case liner products reduces freight expense up to 50% for certain commodities by eliminating the weight and space consumed by ice. In addition to reducing the cost of freight, the removal of ice from the distribution system offers additional benefits as outlined above.

Product enhancements in the fresh-cut vegetable line include fresh-cut vegetable trays designed to look like they were freshly made in the retail grocery store or at home. The rectangular tray design is convenient for storage in consumers' refrigerators and expands the Company's wide-ranging vegetable tray line.

In fiscal year 2007, sales of the value-added retail vegetable tray line and the value-added 12-ounce bag line each grew 18% compared to fiscal year 2006.

Apio has recently entered into an 18-month research and development agreement with Natick Soldier Research, Development & Engineering Center, a branch of the U.S. Military, to develop commercial uses for Landec's BreatheWay packaging technology within the U.S. Military by significantly increasing the shelf life of produce for overseas shipments.

In addition, the Company is in early commercialization for new lines of fresh cut vegetable side dishes, vegetable salads and vegetable snacks.

Agricultural Seed Technology Business

Following the sale of FCD, Landec Ag's strategy is to work closely with Monsanto to further develop its patented, functional polymer coating technology that can be broadly sold and/or licensed to the seed industry. In accordance with its license, supply and R&D agreement with Monsanto, Landec Ag is currently focused on commercializing products for the corn and soybean markets and then plans to broaden its applications to other seed crops.

The Technology and Market Opportunity: Intellicoat Seed Coatings

Landec Ag's Intellicoat seed coating applications are designed to control seed germination timing, increase crop yields, reduce risks and extend crop-planting windows. These coatings are currently available on hybrid corn, soybeans and male inbred corn used for seed production. In fiscal year 2000, Landec Ag launched its first commercial product, Pollinator Plusâ coatings, which is a coating application used by seed companies as a method for spreading pollination to increase yields and reduce risk in the production of hybrid seed corn. There are approximately 650,000 acres of seed production in the United States and in 2007 Pollinator Plus was used by 25 seed companies on approximately 15% of the seed corn production acres in the U.S.

In 2003, Landec Ag commercialized Early Plantâ corn by selling the product directly to farmers through the Fielder's Choice Directâ brand. This application allows farmers to plant into cold soils without the risk of chilling injury, and enables farmers to plant as much as four weeks earlier than normal. With this capability, farmers are able to utilize labor and equipment more efficiently, provide flexibility during the critical planting period and avoid yield losses caused by late planting. In 2007, seven seed companies offered Intellicoat on their hybrid seed corn offerings.

The Business: Landec Ag

Landec Ag had revenues of approximately $2.8 million for the fiscal year ended May 27, 2007, $34.1 million for the fiscal year ended May 28, 2006 and $25.6 million for the fiscal year ended May 29, 2005. Revenues for fiscal year 2007 declined significantly as a result of the sale of FCD on December 1, 2006.

On December 1, 2006, Landec sold FCD, which included the Fielder's Choice Direct® and Heartland Hybrid® brands, to ASI. The acquisition price for FCD was $50 million in cash paid at the close. In addition, the Company could have earned up to an additional $5 million based on FCD results for the twelve months ended May 31, 2007. None of the earn-out was earned. During the fiscal year 2007, Landec recorded income from the sale, net of direct expenses and bonuses, of $22.7 million. The income that was recorded is equal to the difference between the fair value of FCD of $40 million and its net book value, less direct selling expenses and bonuses. In accordance with generally accepted accounting principles, the portion of the $50 million of proceeds in excess of the fair value of FCD, or $10 million, will be allocated to the technology license agreement described below and will be recognized as revenue ratably over the five year term of the technology license agreement or $2 million per year beginning December 1, 2006. The fair value was determined by management with the assistance of an independent appraiser.

On December 1, 2006, Landec also entered into a five-year co-exclusive technology license and polymer supply agreement ("the Agreement") with Monsanto for the use of Landec's Intellicoat polymer seed coating technology. Under the terms of the Agreement, Monsanto will pay Landec $2.6 million per year in exchange for (1) a co-exclusive right to use Landec's Intellicoat temperature activated seed coating technology worldwide during the license period, (2) the right to be the exclusive global sales and marketing agent for the Intellicoat seed coating technology, and (3) the right to purchase the technology any time during the five year term of the Agreement. Monsanto will also fund all operating costs, including all Intellicoat research and development, product development and non-replacement capital costs during the five year agreement period. For the fiscal year ended May 27, 2007, Landec recognized $2.7 million in revenues and income from the Agreement.

The Agreement also provides for a fee payable to Landec of $4 million if Monsanto elects to terminate the agreement or $8 million if Monsanto elects to buyout the technology. If the purchase option is exercised before the fifth anniversary of the Agreement, or if Monsanto elects to terminate the Agreement, all annual license fees and supply payments that have not been paid to Landec will become due upon the purchase. If Monsanto does not exercise its purchase option by the fifth anniversary of the Intellicoat agreement, Landec will receive the termination fee and all rights to the Intellicoat seed coating technology will revert to Landec. Accordingly, Landec will receive minimum guaranteed payments of $17 million for license fees and polymer supply payments over five years or $21 million in maximum payments if Monsanto elects to buyout the licensed technology. The minimum guaranteed payments and the deferred gain of $2 million per year described above will result in Landec recognizing revenue and operating income of $5.4 million per year for fiscal years 2008 through 2011 and $2.7 million per year for fiscal years 2007 and 2012. If Monsanto elects to purchase the technology, an additional $4 million of license fee revenue will be recognized at the time of purchase. If Monsanto exercises its purchase option, Landec and Monsanto will enter into a new long-term supply agreement in which Landec will continue to be the exclusive supplier of Intellicoat polymer materials to Monsanto.

Technology Licensing/Research and Development Businesses

We believe our technology has commercial potential in a wide range of industrial, consumer and medical applications beyond those identified in our core businesses. For example, our core patented technology, Intelimer materials, can be used to trigger catalysts, insecticides or fragrances just by changing the temperature of the Intelimer materials or to activate adhesives through controlled temperature change. In order to exploit these opportunities, we have entered into and will enter into licensing and collaborative corporate agreements for product development and/or distribution in

certain fields. However, given the infrequency and unpredictability of when the Company may enter into any such licensing and research and development arrangements, the Company is unable to disclose its financial expectations in advance of entering into such arrangements.

Industrial Materials and Adhesives

Landec's industrial product development strategy is to focus on coatings, catalysts, resins, additives and adhesives in the polymer materials market. During the product development stage, the Company identifies corporate partners to support the ongoing development and testing of these products, with the ultimate goal of licensing the applications at the appropriate time. Landec's pressure sensitive adhesives ("PSA") technology is currently being evaluated in a variety of industrial and medical applications where strong adhesion to a substrate (i.e. steel, glass, silicon, skin, etc.) is desired for a defined time period and upon thermal triggering, results in a significant peel strength reduction. For example, select PSA systems exhibit greater than 90% reduction in peel strength upon warming, making them ideal for applications on fragile substrates.

Intelimer Polymer Systems

Landec has developed latent catalysts useful in extending pot-life, extending shelf life, reducing waste and improving thermoset cure methods. Some of these latent catalysts are currently being distributed by Akzo-Nobel Chemicals B.V. through a licensing agreement with Air Products. The Company has also developed Intelimer polymer materials useful in enhancing the formulating options for various personal care products. The rights to develop and sell Landec's latent catalysts and personal care technologies were licensed to Air Products in March 2006.

Personal Care and Cosmetic Applications

Landec's personal care and cosmetic applications strategy is focused on supplying Intelimer materials to industry leaders for use in lotions and creams, and potentially color cosmetics, lipsticks and hair care. The Company's partner, Air Products, is currently shipping products to L'Oreal for use in lotions and creams. Sales of Landec materials used in L'Oreal products have not been material to the Company's financials.

Medical Applications

On December 23, 2005, Landec entered into an exclusive licensing agreement with Aesthetic Sciences Corporation ("Aesthetic Sciences"). Aesthetic Sciences paid Landec an upfront license fee of $250,000 for the exclusive rights to use Landec's Intelimer materials technology for the development of dermal fillers worldwide. Landec will also receive royalties on the sale of products incorporating Landec's technology. In addition, the Company has received shares of preferred stock valued at $1.8 million which represents a 19.9% ownership interest in Aesthetic Sciences. At this time, the Company is unable to predict the ultimate outcome of the collaboration with Aesthetic Sciences and the timing or amount of future revenues, if any.

Sales and Marketing

Each of the Company's core businesses are supported by dedicated sales and marketing resources. The Company intends to develop its internal sales capacity as more products progress toward commercialization and as business volume expands geographically**.** During fiscal years 2007, 2006 and 2005, sales to the Company's top five customers accounted for approximately 50%, 46% and 42%, respectively, of its revenues, with the top customer, Costco Wholesale Corp., accounting for approximately 21%, 16% and 15%, respectively, of the Company's revenues.

Food Products Technology Business

Apio has 20 sales people, located in central California and throughout the U.S., supporting the export business and the specialty packaged value-added produce business.

Seasonality

The Company's sales are moderately seasonal. Prior to the sale of FCD, Landec Ag revenues and profits were concentrated over a few months during the spring planting season (generally during the Company's third and fourth quarters). In addition, Apio can be heavily affected by seasonal weather factors which have impacted quarterly results, such as high cost of sourcing product in June/July 2006 and January 2007 due to a shortage of essential value-added produce items.

Manufacturing and Processing

Food Products Technology Business

The manufacturing process for the Company's proprietary BreatheWay packaging products is comprised of polymer manufacturing, membrane manufacturing and label package conversion. A third party toll manufacturer currently makes virtually all of the polymers for the BreatheWay packaging. Select outside contractors currently manufacture the breathable membranes and Landec has transitioned virtually all of the label package conversion to Apio’s Guadalupe facility to meet the increasing product demand and to provide additional developmental capabilities.

Apio processes virtually all of its fresh-cut value-added products in its state-of-the-art processing facility located in Guadalupe, California. Cooling of produce is done through third parties and Apio Cooling LP, a separate company in which Apio has a 60% ownership interest and is the general partner.

Agricultural Seed Technology Business

The Company performs its batch coating operations in a leased facility in Oxford, Indiana. This facility is being used to coat other seed companies’ inbred seed corn with the Company’s Pollinator Plus seed corn coatings.

The Company has a pilot manufacturing facility in Indiana to support the commercialization of Early Plant corn and for the Relay Cropping System for wheat/coated soybean products. This facility utilizes a continuous coating process that has increased seed coating capabilities by over tenfold compared to the previous system using batch coaters.

General

Many of the raw materials used in manufacturing certain of the Company’s products are currently purchased from a single source, including certain monomers used to synthesize Intelimer polymers and substrate materials for the Company’s breathable membranes. Upon manufacturing scale-up of seed coating operations, the Company may enter into alternative supply arrangements. Although to date the Company has not experienced difficulty acquiring materials for the manufacture of its products, no assurance can be given that interruptions in supplies will not occur in the future, that the Company will be able to obtain substitute vendors, or that the Company will be able to procure comparable materials at similar prices and terms within a reasonable time. Any such interruption of supply could have a material adverse effect on the Company’s ability to manufacture and distribute its products and, consequently, could materially and adversely affect the Company’s business, operating results and financial condition.

Research and Development

Landec is focusing its research and development resources on both existing and new applications of its Intelimer technology. Expenditures for research and development for the fiscal years ended May 27, 2007, May 28, 2006 and May 29, 2005 were $3.1 million, $3.0 million and $2.5 million, respectively. Research and development expenditures funded by corporate partners were $661,000 for the fiscal year ended May 27, 2007, $100,000 for the fiscal year ended May 28, 2006 and $20,000 for the fiscal year ended May 29, 2005. The Company may continue to seek funds for applied materials research programs from U.S. government agencies as well as from commercial entities. The Company anticipates that it will continue to have significant research and development expenditures in order to maintain its competitive position with a continuing flow of innovative, high-quality products and services. As of May 27, 2007, Landec had 22 employees engaged in research and development with experience in polymer and analytical chemistry, product application, product formulation, mechanical and chemical engineering.

Competition

The Company operates in highly competitive and rapidly evolving fields, and new developments are expected to continue at a rapid pace. Competition from large food packaging and agricultural companies is intense. In addition, the nature of the Company's collaborative arrangements and its technology licensing business may result in its corporate partners and licensees becoming competitors of the Company. Many of these competitors have substantially greater financial and technical resources and production and marketing capabilities than the Company, and many have substantially greater experience in conducting field trials, obtaining regulatory approvals and manufacturing and marketing commercial products. There can be no assurance that these competitors will not succeed in developing alternative technologies and products that are more effective, easier to use or less expensive than those which have been or are being developed by the Company or that would render the Company's technology and products obsolete and non-competitive.

Patents and Proprietary Rights

The Company's success depends in large part on its ability to obtain patents, maintain trade secret protection and operate without infringing on the proprietary rights of third parties. The Company has had 33 U.S. patents issued of which 27 remain active as of May 27, 2007 with expiration dates ranging from 2010 to 2022. The Company's issued patents include claims relating to compositions, devices and use of a class of temperature sensitive polymers that exhibit distinctive properties of permeability, adhesion and viscosity control. There can be no assurance that any of the pending patent applications will be approved, that the Company will develop additional proprietary products that are patentable, that any patents issued to the Company will provide the Company with competitive advantages or will not be challenged by any third parties or that the patents of others will not prevent the commercialization of products incorporating the Company's technology. Furthermore, there can be no assurance that others will not independently develop similar products, duplicate any of the Company's products or design around the Company's patents. Any of the foregoing results could have a material adverse effect on the Company's business, operating results and financial condition.

The commercial success of the Company will also depend, in part, on its ability to avoid infringing patents issued to others. The Company has received, and may in the future receive, from third parties, including some of its competitors, notices claiming that it is infringing third party patents or other proprietary rights. If the Company were determined to be infringing any third-party patent, the Company could be required to pay damages, alter its products or processes, obtain licenses or cease certain activities. In addition, if patents are issued to others which contain claims that compete or conflict with those of the Company and such competing or conflicting claims are ultimately determined to be valid, the Company may be required to pay damages, to obtain licenses to these patents, to develop or obtain alternative technology or to cease using such technology. If the Company is required to obtain any licenses, there can be no assurance that the Company will be able to do so on commercially favorable terms, if at all. The Company's failure to obtain a license to any technology that it may require to commercialize its products could have a material adverse impact on the Company's business, operating results and financial condition.

Litigation, which could result in substantial costs to the Company, may also be necessary to enforce any patents issued or licensed to the Company or to determine the scope and validity of third-party proprietary rights. If competitors of the Company prepare and file patent applications in the United States that claim technology also claimed by the Company, the Company may have to participate in interference proceedings declared by the U.S. Patent and Trademark Office to determine priority of invention, which could result in substantial cost to and diversion of effort by the Company, even if the eventual outcome is favorable to the Company. Any such litigation or interference proceeding, regardless of outcome, could be expensive and time consuming and could subject the Company to significant liabilities to third parties, require disputed rights to be licensed from third parties or require the Company to cease using such technology and consequently, could have a material adverse effect on the Company's business, operating results and financial condition.

In addition to patent protection, the Company also relies on trade secrets, proprietary know-how and technological advances which the Company seeks to protect, in part, by confidentiality agreements with its collaborators, employees and consultants. There can be no assurance that these agreements will not be breached, that the Company will have adequate remedies for any breach, or that the Company's trade secrets and proprietary know-how will not otherwise become known or be independently discovered by others.

Employees

As of May 27, 2007, Landec had 107 full-time employees, of whom 52 were dedicated to research, development, manufacturing, quality control and regulatory affairs and 55 were dedicated to sales, marketing and administrative activities. Landec intends to recruit additional personnel in connection with the development, manufacturing and marketing of its products. None of Landec's employees is represented by a union, and Landec believes relationships with its employees are good.

Available Information

Landec's Web site is http://www.landec.com. Landec makes available free of charge its annual, quarterly and current reports, and any amendments to those reports, as soon as reasonably practicable after electronically filing such reports with the SEC. Information contained on our website is not part of this Report.

Item 1A. ***Risk Factors***

Landec desires to take advantage of the "Safe Harbor" provisions of the Private Securities Litigation Reform Act of 1995 and of Section 21E and Rule 3b-6 under the Securities Exchange Act of 1934. Specifically, Landec wishes to alert readers that the following important factors, as well as other factors including, without limitation, those described elsewhere in this report, could in the future affect, and in the past have affected, Landec's actual results and could cause Landec's results for future periods to differ materially from those expressed in any forward-looking statements made by or on behalf of Landec. Landec assumes no obligation to update such forward-looking statements.

Our Future Operating Results Are Likely to Fluctuate Which May Cause Our Stock Price to Decline

In the past, our results of operations have fluctuated significantly from quarter to quarter and are expected to continue to fluctuate in the future. Historically, Landec Ag has been the primary source of these fluctuations, as its revenues and profits have been concentrated over a few months during the spring planting season (generally during our third and fourth fiscal quarters). In addition, Apio can be heavily affected by seasonal and weather factors which have impacted quarterly results, such as the high cost of sourcing product in June/July 2006 and January 2007 due to a shortage of essential value-added produce items. Our earnings may also fluctuate based on our ability to collect accounts receivables from customers and note receivables from growers and on price fluctuations in the fresh vegetables and fruits markets. Other factors that affect our food and/or agricultural operations include:

- the seasonality of our supplies;
- our ability to process produce during critical harvest periods;
- the timing and effects of ripening;
- the degree of perishability;
- the effectiveness of worldwide distribution systems;
- total worldwide industry volumes;
- the seasonality of consumer demand;
- foreign currency fluctuations; and

- foreign importation restrictions and foreign political risks.

As a result of these and other factors, we expect to continue to experience fluctuations in quarterly operating results.

We May Not Be Able to Achieve Acceptance of Our New Products in the Marketplace

Our success in generating significant sales of our products will depend in part on the ability of us and our partners and licensees to achieve market acceptance of our new products and technology. The extent to which, and rate at which, we achieve market acceptance and penetration of our current and future products is a function of many variables including, but not limited to:

- price;
- safety;
- efficacy;
- reliability;
- conversion costs;
- marketing and sales efforts; and
- general economic conditions affecting purchasing patterns.

We may not be able to develop and introduce new products and technologies in a timely manner or new products and technologies may not gain market acceptance. We are in the early stage of product commercialization of certain Intelimer-based specialty packaging, Intellicoat seed coatings and other Intelimer polymer products and many of our potential products are in development. We believe that our future growth will depend in large part on our ability to develop and market new products in our target markets and in new markets. In particular, we expect that our ability to compete effectively with existing food products, agricultural, industrial and medical companies will depend substantially on successfully developing, commercializing, achieving market acceptance of and reducing the cost of producing our products. In addition, commercial applications of our temperature switch polymer technology are relatively new and evolving. Our failure to develop new products or the failure of our new products to achieve market acceptance would have a material adverse effect on our business, results of operations and financial condition.

We Face Strong Competition in the Marketplace

Competitors may succeed in developing alternative technologies and products that are more effective, easier to use or less expensive than those which have been or are being developed by us or that would render our technology and products obsolete and non-competitive. We operate in highly competitive and rapidly evolving fields, and new developments are expected to continue at a rapid pace. Competition from large food products, agricultural, industrial and medical companies is expected to be intense. In addition, the nature of our collaborative arrangements may result in our corporate partners and licensees becoming our competitors. Many of these competitors have substantially greater financial and technical resources and production and marketing capabilities than we do, and may have substantially greater experience in conducting clinical and field trials, obtaining regulatory approvals and manufacturing and marketing commercial products.

We Have a Concentration of Manufacturing in One Location for Apio and May Have to Depend on Third Parties to Manufacture Our Products

Any disruptions in our primary manufacturing operation at Apio’s facility in Guadalupe, California would reduce our ability to sell our products and would have a material adverse effect on our financial results. Additionally, we may

need to consider seeking collaborative arrangements with other companies to manufacture our products. If we become dependent upon third parties for the manufacture of our products, our profit margins and our ability to develop and deliver those products on a timely basis may be affected. Failures by third parties may impair our ability to deliver products on a timely basis and impair our competitive position. We may not be able to continue to successfully operate our manufacturing operations at acceptable costs, with acceptable yields, and retain adequately trained personnel.

Our Dependence on Single-Source Suppliers and Service Providers May Cause Disruption in Our Operations Should Any Supplier Fail to Deliver Materials

We may experience difficulty acquiring materials or services for the manufacture of our products or we may not be able to obtain substitute vendors. We may not be able to procure comparable materials at similar prices and terms within a reasonable time. Several services that are provided to Apio are obtained from a single provider. Several of the raw materials we use to manufacture our products are currently purchased from a single source, including some monomers used to synthesize Intelimer polymers and substrate materials for our breathable membrane products. Any interruption of our relationship with single-source suppliers or service providers could delay product shipments and materially harm our business.

We May Be Unable to Adequately Protect Our Intellectual Property Rights

We may receive notices from third parties, including some of our competitors, claiming infringement by our products of patent and other proprietary rights. Regardless of their merit, responding to any such claim could be time-consuming, result in costly litigation and require us to enter royalty and licensing agreements which may not be offered or available on terms acceptable to us. If a successful claim is made against us and we fail to develop or license a substitute technology, we could be required to alter our products or processes and our business, results of operations or financial position could be materially adversely affected. Our success depends in large part on our ability to obtain patents, maintain trade secret protection and operate without infringing on the proprietary rights of third parties. Any pending patent applications we file may not be approved and we may not be able to develop additional proprietary products that are patentable. Any patents issued to us may not provide us with competitive advantages or may be challenged by third parties. Patents held by others may prevent the commercialization of products incorporating our technology. Furthermore, others may independently develop similar products, duplicate our products or design around our patents.

Our Operations Are Subject to Regulations that Directly Impact Our Business

Our food packaging products are subject to regulation under the Food, Drug and Cosmetic Act (the “FDC Act”). Under the FDC Act, any substance that when used as intended may reasonably be expected to become, directly or indirectly, a component or otherwise affect the characteristics of any food may be regulated as a food additive unless the substance is generally recognized as safe. We believe that food packaging materials are generally not considered food additives by the FDA because these products are not expected to become components of food under their expected conditions of use. We consider our breathable membrane product to be a food packaging material not subject to regulation or approval by the FDA. We have not received any communication from the FDA concerning our breathable membrane product. If the FDA were to determine that our breathable membrane products are food additives, we may be required to submit a food additive petition for approval by the FDA. The food additive petition process is lengthy, expensive and uncertain. A determination by the FDA that a food additive petition is necessary would have a material adverse effect on our business, operating results and financial condition.

Federal, state and local regulations impose various environmental controls on the use, storage, discharge or disposal of toxic, volatile or otherwise hazardous chemicals and gases used in some of the manufacturing processes. Our failure to control the use of, or to restrict adequately the discharge of, hazardous substances under present or future regulations could subject us to substantial liability or could cause our manufacturing operations to be suspended and changes in environmental regulations may impose the need for additional capital equipment or other requirements.

Our agricultural operations are subject to a variety of environmental laws including, the Food Quality Protection Act of 1966, the Clean Air Act, the Clean Water Act, the Resource Conservation and Recovery Act, the Federal Insecticide, Fungicide and Rodenticide Act, and the Comprehensive Environmental Response, Compensation and Liability Act. Compliance with these laws and related regulations is an ongoing process. Environmental concerns are,

however, inherent in most agricultural operations, including those we conduct. Moreover, it is possible that future developments, such as increasingly strict environmental laws and enforcement policies could result in increased compliance costs.

The Company is subject to the Perishable Agricultural Commodities Act (“PACA”) law. PACA regulates fair trade standards in the fresh produce industry and governs all the products sold by Apio. Our failure to comply with the PACA requirements could among other things, result in civil penalties, suspension or revocation of a license to sell produce, and in the most egregious cases, criminal prosecution, which could have a material adverse effect on our business.

Adverse Weather Conditions and Other Acts of God May Cause Substantial Decreases in Our Sales and/or Increases in Our Costs

Our Food Products business is subject to weather conditions that affect commodity prices, crop yields, and decisions by growers regarding crops to be planted. Crop diseases and severe conditions, particularly weather conditions such as floods, droughts, frosts, windstorms, earthquakes and hurricanes, may adversely affect the supply of vegetables and fruits used in our business, which could reduce the sales volumes and/or increase the unit production costs. Because a significant portion of the costs are fixed and contracted in advance of each operating year, volume declines due to production interruptions or other factors could result in increases in unit production costs which could result in substantial losses and weaken our financial condition.

We Depend on Strategic Partners and Licenses for Future Development

Our strategy for development, clinical and field testing, manufacture, commercialization and marketing for some of our current and future products includes entering into various collaborations with corporate partners, licensees and others. We are dependent on our corporate partners to develop, test, manufacture and/or market some of our products. Although we believe that our partners in these collaborations have an economic motivation to succeed in performing their contractual responsibilities, the amount and timing of resources to be devoted to these activities are not within our control. Our partners may not perform their obligations as expected or we may not derive any additional revenue from the arrangements. Our partners may not pay any additional option or license fees to us or may not develop, market or pay any royalty fees related to products under the agreements. Moreover, some of the collaborative agreements provide that they may be terminated at the discretion of the corporate partner, and some of the collaborative agreements provide for termination under other circumstances. Our partners may pursue existing or alternative technologies in preference to our technology. Furthermore, we may not be able to negotiate additional collaborative arrangements in the future on acceptable terms, if at all, and our collaborative arrangements may not be successful.

Both Domestic and Foreign Government Regulations Can Have an Adverse Effect on Our Business Operations

Our products and operations are subject to governmental regulation in the United States and foreign countries. The manufacture of our products is subject to periodic inspection by regulatory authorities. We may not be able to obtain necessary regulatory approvals on a timely basis or at all. Delays in receipt of or failure to receive approvals or loss of previously received approvals would have a material adverse effect on our business, financial condition and results of operations. Although we have no reason to believe that we will not be able to comply with all applicable regulations regarding the manufacture and sale of our products and polymer materials, regulations are always subject to change and depend heavily on administrative interpretations and the country in which the products are sold. Future changes in regulations or interpretations relating to matters such as safe working conditions, laboratory and manufacturing practices, environmental controls, and disposal of hazardous or potentially hazardous substances may adversely affect our business.

We are subject to USDA rules and regulations concerning the safety of the food products handled and sold by Apio, and the facilities in which they are packed and processed. Failure to comply with the applicable regulatory requirements can, among other things, result in:

- fines, injunctions, civil penalties, and suspensions,
- withdrawal of regulatory approvals,
- product recalls and product seizures, including cessation of manufacturing and sales,
- operating restrictions, and

- criminal prosecution.

We may be required to incur significant costs to comply with the laws and regulations in the future which may have a material adverse effect on our business, operating results and financial condition.

Our International Operations and Sales May Expose Our Business to Additional Risks

For the fiscal year ended May 27, 2007, approximately 22% of our total revenues were derived from product sales to international customers. A number of risks are inherent in international transactions. International sales and operations may be limited or disrupted by any of the following:

- regulatory approval process,
- government controls,
- export license requirements,
- political instability,
- price controls,
- trade restrictions,
- changes in tariffs, or
- difficulties in staffing and managing international operations.

Foreign regulatory agencies have or may establish product standards different from those in the United States, and any inability to obtain foreign regulatory approvals on a timely basis could have a material adverse effect on our international business, and our financial condition and results of operations. While our foreign sales are currently priced in dollars, fluctuations in currency exchange rates may reduce the demand for our products by increasing the price of our products in the currency of the countries to which the products are sold. Regulatory, geopolitical and other factors may adversely impact our operations in the future or require us to modify our current business practices.

Cancellations or Delays of Orders by Our Customers May Adversely Affect Our Business

During fiscal year 2007, sales to our top five customers accounted for approximately 50% of our revenues, with our largest customer, Costco Wholesale Corp. accounting for approximately 21% of our revenues. We expect that, for the foreseeable future, a limited number of customers may continue to account for a substantial portion of our net revenues. We may experience changes in the composition of our customer base as we have experienced in the past. We do not have long-term purchase agreements with any of our customers. The reduction, delay or cancellation of orders from one or more major customers for any reason or the loss of one or more of our major customers could materially and adversely affect our business, operating results and financial condition. In addition, since some of the products processed by Apio at its Guadalupe, California facility are sole sourced to its customers, our operating results could be adversely affected if one or more of our major customers were to develop other sources of supply. Our current customers may not continue to place orders, orders by existing customers may be canceled or may not continue at the levels of previous periods or we may not be able to obtain orders from new customers.

Our Sale of Some Products May Increase Our Exposure to Product Liability Claims

The testing, manufacturing, marketing, and sale of the products we develop involve an inherent risk of allegations of product liability. If any of our products were determined or alleged to be contaminated or defective or to have caused a harmful accident to an end-customer, we could incur substantial costs in responding to complaints or litigation regarding our products and our product brand image could be materially damaged. Either event may have a material adverse effect on our business, operating results and financial condition. Although we have taken and intend to continue to take what we believe are appropriate precautions to minimize exposure to product liability claims, we may not be able to avoid significant liability. We currently maintain product liability insurance. While we believe the coverage and limits are consistent with industry standards, our coverage may not be adequate or may not continue to be available at an acceptable cost, if at all. A product liability claim, product recall or other claim with respect to uninsured liabilities or in excess of insured liabilities could have a material adverse effect on our business, operating results and financial condition.

Our Stock Price May Fluctuate in Accordance with Market Conditions

The following events may cause the market price of our common stock to fluctuate significantly:

- technological innovations applicable to our products,
- our attainment of (or failure to attain) milestones in the commercialization of our technology,
- our development of new products or the development of new products by our competitors,
- new patents or changes in existing patents applicable to our products,
- our acquisition of new businesses or the sale or disposal of a part of our businesses,
- development of new collaborative arrangements by us, our competitors or other parties,
- changes in government regulations applicable to our business,
- changes in investor perception of our business,
- fluctuations in our operating results and
- changes in the general market conditions in our industry.

These broad fluctuations may adversely affect the market price of our common stock.

Since We Order Cartons and Film for Our Products from Suppliers in Advance of Receipt of Customer Orders for Such Products, We Could Face a Material Inventory Risk

As part of our inventory planning, we enter into negotiated orders with vendors of cartons and film used for packing our products in advance of receiving customer orders for such products. Accordingly, we face the risk of ordering too many cartons and film since orders are generally based on forecasts of customer orders rather than actual orders. If we cannot change or be released from the orders, we may incur costs as a result of inadequately predicting cartons and film orders in advance of customer orders. Because of this, we may have an oversupply of cartons and film and face the risk of not being able to sell such inventory and our anticipated reserves for losses may be inadequate if we have misjudged the demand for our products. Our business and operating results could be adversely affected as a result of these increased costs.

Recently Enacted Changes in Securities Laws and Regulations Have and Will Continue to Increase Our Costs

The Sarbanes-Oxley Act of 2002 (the “Act”) that became law in July 2002 required changes in some of our corporate governance, public disclosure and compliance practices. In addition, NASDAQ has imposed additional requirements for companies, such as Landec, that are listed on The NASDAQ Global Select Market. These developments have increased our legal and financial compliance costs. These changes could make it more difficult and more expensive for us to obtain director and officer liability insurance, and we may be required to accept reduced coverage or incur substantially higher costs to obtain coverage. These developments could make it more difficult for us to attract and retain qualified members for our board of directors and to serve on our audit committee.

Our Controlling Shareholders Exert Significant Influence over Corporate Events that May Conflict with the Interests of Other Shareholders

Our executive officers and directors and their affiliates own or control approximately 17% of our common stock (including options exercisable within 60 days). Accordingly, these officers, directors and shareholders may have the ability to exert significant influence over the election of our Board of Directors, the approval of amendments to our articles and bylaws and the approval of mergers or other business combination transactions requiring shareholder approval. This concentration of ownership may have the effect of delaying or preventing a merger or other business combination transaction, even if the transaction or amendments would be beneficial to our other shareholders. In addition, our controlling shareholders may approve amendments to our articles or bylaws to implement anti-takeover or management friendly provisions that may not be beneficial to our other shareholders.

We May Be Exposed to Employment Related Claims and Costs that Could Materially Adversely Affect Our Business

We have been subject in the past, and may be in the future, to claims by employees based on allegations of discrimination, negligence, harassment and inadvertent employment of illegal aliens or unlicensed personnel, and we may be subject to payment of workers' compensation claims and other similar claims. We could incur substantial costs and our management could spend a significant amount of time responding to such complaints or litigation regarding employee claims, which may have a material adverse effect on our business, operating results and financial condition.

We Are Dependent on Our Key Employees and if One or More of Them Were to Leave, We Could Experience Difficulties in Replacing Them and Our Operating Results Could Suffer

The success of our business depends to a significant extent upon the continued service and performance of a relatively small number of key senior management, technical, sales, and marketing personnel. The loss of any of our key personnel would likely harm our business. In addition, competition for senior level personnel with knowledge and experience in our different lines of business is intense. If any of our key personnel were to leave, we would need to devote substantial resources and management attention to replace them. As a result, management attention may be diverted from managing our business, and we may need to pay higher compensation to replace these employees.

We May Issue Preferred Stock with Preferential Rights that Could Affect Your Rights

Our Board of Directors has the authority, without further approval of our shareholders, to fix the rights and preferences, and to issue shares, of preferred stock. In November 1999, we issued and sold shares of Series A Convertible Preferred Stock and in October 2001 we issued and sold shares of Series B Convertible Preferred Stock. The Series A Convertible Preferred Stock was converted into 1,666,670 shares of Common Stock on November 19, 2002 and the Series B Convertible Preferred Stock was converted into 1,744,102 shares of Common Stock on May 7, 2004.

The issuance of new shares of preferred stock could have the effect of making it more difficult for a third party to acquire a majority of our outstanding stock, and the holders of such preferred stock could have voting, dividend, liquidation and other rights superior to those of holders of our Common Stock.

We Have Never Paid any Dividends on Our Common Stock

We have not paid any cash dividends on our Common Stock since inception and do not expect to do so in the foreseeable future. Any dividends may be subject to preferential dividends payable on any preferred stock we may issue.

Our Profitability Could Be Materially and Adversely Affected if it Is Determined that the Book Value of Goodwill is Higher than Fair Value

Our balance sheet includes an amount designated as “goodwill” that represents a portion of our assets and our shareholders’ equity. Goodwill arises when an acquirer pays more for a business than the fair value of the tangible and separately measurable intangible net assets. Under Statement of Financial Accounting Standards No. 142 “Goodwill and Other Intangible Assets”, beginning in fiscal year 2002, the amortization of goodwill has been replaced with an “impairment test” which requires that we compare the fair value of goodwill to its book value at least annually and more frequently if circumstances indicate a possible impairment. If we determine at any time in the future that the book value of goodwill is higher than fair value then the difference must be written-off, which could materially and adversely affect our profitability.

1B. Unresolved Staff Comments

None.

Item 2. ***Properties***

As of May 27, 2007, the Company owned or leased properties in Menlo Park, Arroyo Grande and Guadalupe, California; West Lebanon and Oxford Indiana.

These properties are described below:

Location	Business Segment	Ownership	Facilities	Acres of Land	Lease Expiration
Menlo Park, CA	Other	Leased	10,400 square feet of office and laboratory space	—	12/31/09
West Lebanon, IN	Agricultural Seed Technology	Owned	4,000 square feet of warehouse and manufacturing space	—	—
Oxford, IN	Agricultural Seed Technology	Leased	13,400 square feet of laboratory and manufacturing space	—	6/30/08
Guadalupe, CA	Food Products Technology	Owned	142,000 square feet of office space, manufacturing and cold storage	17.7	—
Arroyo Grande, CA	Food Products Technology	Leased	1,100 square feet of office space	—	6/30/08

There are no bank liens encumbering any of the Company's owned land and buildings.

Item 3. ***Legal Proceedings***

The Company is involved in litigation arising in the normal course of business. The Company is not a party to any legal proceedings which would result in the payment of any amounts that would be material to the business or financial condition of the Company.

Item 4. ***Submission of Matters to a Vote of Security Holders***

There were no matters submitted to a vote of security holders during the fourth quarter of the Company's fiscal year ended May 27, 2007.

PART II

Item 5. ***Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities***

Market Information

The Common Stock is traded on The NASDAQ Global Select Market under the symbol "LNDC". The following table sets forth for each period indicated the high and low sales prices for the Common Stock.

Fiscal Year Ended May 27, 2007		High		Low
4th Quarter ending May 27, 2007	$	15.13	$	12.01
3rd Quarter ending February 25, 2007	$	13.80	$	9.49
2nd Quarter ending November 26, 2006	$	11.32	$	9.03
1st Quarter ending August 27, 2006	$	11.11	$	7.96
Fiscal Year Ended May 28, 2006		High		Low
4th Quarter ending May 28, 2006	$	9.65	$	6.71
3rd Quarter ending February 26, 2006	$	7.84	$	6.23
2nd Quarter ending November 27, 2005	$	8.01	$	6.32
1st Quarter ending August 28, 2005	$	6.98	$	6.66

Holders

There were approximately 80 holders of record of 25,904,212 shares of outstanding Common Stock as of July 13, 2007. Since certain holders are listed under their brokerage firm's names, the actual number of shareholders is higher.

Dividends

The Company has not paid any dividends on the Common Stock since its inception. The Company presently intends to retain all future earnings, if any, for its business and does not anticipate paying cash dividends on its Common Stock in the foreseeable future.

Issuer Purchases of Equity Securities

There were no shares repurchased by the Company during the quarter ending on May 27, 2007.

Item 6. ***Selected Financial Data***

The information set forth below is not necessarily indicative of the results of future operations and should be read in conjunction with the information contained in Item 7 - "Management's Discussion and Analysis of Financial Condition and Results of Operations" and the Consolidated Financial Statements and Notes to Consolidated Financial Statements contained in Item 8 of this report.

	Year Ended May 27, 2007	Year Ended May 28, 2006	Year Ended May 29, 2005	Year Ended May 30, 2004	Seven Months Ended May 25, 2003	Seven Months Ended June 2, 2002 (unaudited)	Year Ended October 27, 2002
Statement of Operations Data: (in thousands)							
Revenues:							
Product sales	$ 201,892	$ 225,404	$ 201,020	$ 185,664	$ 98,689	$ 96,513	$ 152,958
Service revenues	3,539	3,725	3,704	5,791	12,784	15,882	26,827
License fees	4,013	2,398	88	88	357	1,274	2,330
R&D and royalty revenues	1,054	426	418	549	429	402	1,040
Total revenues	210,498	231,953	205,230	192,092	112,259	114,071	183,155
Cost of revenue:							
Cost of product sales	175,252	188,904	170,359	158,911	82,339	80,680	131,352
Cost of service revenue	2,860	3,005	2,899	3,390	9,216	12,505	20,463
Total cost of revenue	178,112	191,909	173,258	162,301	91,555	93,185	151,815
Gross profit	32,386	40,044	31,972	29,791	20,704	20,886	31,340
Operating costs and expenses:							
Research and development	3,074	3,042	2,543	3,452	2,118	2,018	3,532
Selling, general and administrative	21,616	27,979	23,412	22,284	15,185	16,293	26,114
Income from sale of FCD	(22,669)	—	—	—	—	—	—
Exit domestic commodity vegetable business	—	—	—	—	1,095	—	—
Total operating costs and expenses	2,021	31,021	25,955	25,736	18,398	18,311	29,646
Operating profit	30,365	9,023	6,017	4,055	2,306	2,575	1,694
Interest income	1,945	633	214	164	144	177	247
Interest expense	(251)	(452)	(414)	(811)	(642)	(1,097)	(1,551)
Minority interest expense	(412)	(529)	(411)	(537)	(235)	(224)	(525)
Other (expense)/income, net	(2)	(24)	(4)	29	218	71	336
Income from continuing operations before taxes	31,645	8,651	5,402	2,900	1,791	1,502	201
Income tax expense	(2,456)	—	—	—	—	—	—

Income from continuing operations	29,189	8,651	5,402	2,900	1,791	1,502	201
Discontinued operations:							
Loss from discontinued operations	—	—	—	—	—	—	—
Loss on disposal of operations	—	—	—	—	—	—	(1,688)
Loss from discontinued operations	—	—	—	—	—	—	(1,688)
Net income (loss)	$ 29,189	$ 8,651	$ 5,402	$ 2,900	$ 1,791	$ 1,502	$ (1,487)
Net income (loss)	$ 29,189	$ 8,651	$ 5,402	$ 2,900	$ 1,791	$ 1,502	$ (1,487)
Dividends on preferred stock	—	—	—	(464)	(219)	(202)	(412)
Net income (loss) applicable to common shareholders	$ 29,189	$ 8,651	$ 5,402	$ 2,436	$ 1,572	$ 1,300	$ (1,899)

Statements of Operations Data: (in thousands, except per share data)	**Year Ended May 27, 2007**	**Year Ended May 28, 2006**	**Year Ended May 29, 2005**	**Year Ended May 30, 2004**	**Seven Months Ended May 25, 2003**	**Seven Months Ended June 2, 2002** (Unaudited)	**Year Ended October 27, 2002**
Basic net income (loss) per share:							
Continuing operations	$ 1.16	$ 0.35	$ 0.23	$ 0.11	$ 0.08	$ 0.07	$ (0.01)
Discontinued operations	—	—	—	—	—	—	(0.09)
Basic net income (loss) per share	$ 1.16	$ 0.35	$ 0.23	$ 0.11	$ 0.08	$ 0.07	$ (0.10)
Diluted net income (loss) per share:							
Continuing operations	$ 1.07	$ 0.32	$ 0.21	$ 0.12	$ 0.07	$ 0.06	$ (0.01)
Discontinued operations	—	—	—	—	—	—	(0.09)
Diluted net income (loss) per share	$ 1.07	$ 0.32	$ 0.21	$ 0.12	$ 0.07	$ 0.06	$ (0.10)
Shares used in per share computation:							
Basic	25,260	24,553	23,705	21,396	20,948	17,777	18,172
Diluted	26,558	25,657	24,614	23,556	22,626	21,082	18,172

Balance Sheet Data: (in thousands)	**May 27, 2007**	**May 28, 2006**	**May 29, 2005**	**May 30, 2004**	**May 25, 2003**	**October 27, 2002**
Cash and cash equivalents	$ 62,556	$ 15,164	$ 7,426	$ 4,966	$ 3,610	$ 7,813
Total assets	141,368	119,025	100,075	93,007	96,887	107,803
Debt	28	2,018	3,088	8,996	13,494	17,543
Convertible preferred stock	—	—	—	—	5,531	14,461
Accumulated deficit	(19,332)	(41,239)	(49,890)	(55,292)	(57,728)	(59,300)
Total shareholders' equity	$ 110,228	$ 85,049	$ 72,060	$ 61,549	$ 57,903	$ 55,963

Item 7. ***Management's Discussion and Analysis of Financial Condition and Results of Operations***

The following discussion should be read in conjunction with the Company's Consolidated Financial Statements contained in Item 8 of this report. Except for the historical information contained herein, the matters discussed in this report are forward-looking statements within the meaning of Section 21E of the Securities Exchange Act of 1934. These forward-looking statements involve certain risks and uncertainties that could cause actual results to differ materially from those in the forward-looking statements. Potential risks and uncertainties include, without limitation, those mentioned in this report and, in particular, the factors described in Item 1A. "Risk Factors." Landec undertakes no obligation to revise any forward-looking statements in order to reflect events or circumstances that may arise after the date of this report.

Overview

Since its inception in October 1986, the Company has been engaged in the research and development of its Intelimer technology and related products. The Company has launched four product lines from this core development - QuickCast™ splints and casts, in April 1994, which was subsequently sold to Bissell Healthcare Corporation in August 1997; Intelimer packaging technology for the fresh-cut and whole produce packaging market, in September 1995; Intelimer Polymer Systems in June 1997 that includes polymer materials for various industrial applications and beginning in November 2003 for personal care applications; and Intellicoat coated corn seeds in the Fall of 1999.

With the acquisition of Apio in 1999 and Landec Ag in 1997, the Company has focused on two core businesses - Food Products Technology and Agricultural Seed Technology. The Food Products Technology segment combines the Company's Intelimer packaging technology with Apio's fresh-cut and whole produce business. Prior to the sale of FCD on December 1, 2006 to ASI, the Agricultural Seed Technology segment integrated the Intellicoat seed coating technology with FCD's direct marketing, telephone sales and distribution capabilities. The Company also operates a Technology Licensing/Research and Development business which develops products to be licensed outside of the Company's core businesses. See "Business - Description of Core Business".

From inception through May 27, 2007, the Company's accumulated deficit was $19.3 million. The Company may incur additional losses in the future. The amount of future net profits, if any, is uncertain and there can be no assurance that the Company will be able to sustain profitability in future years.

Critical Accounting Policies and Use of Estimates

Use of Estimates

The preparation of the Company's financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ materially from those estimates. The judgments and assumptions used by management are based on historical experience and other factors, which are believed to be reasonable under the circumstances.

Notes and Advances Receivables

Apio has made advances to produce growers for crop and harvesting costs. Typically these advances are paid off within the growing season (less than one year) from harvested crops. Advances not fully paid during the current growing season are converted to interest bearing obligations, evidenced by contracts and notes receivable. These notes receivable and advances are secured by liens on land and/or crops and have terms that range from twelve to sixty months. Notes receivable are periodically reviewed (at least quarterly) for collectibility. A reserve is established for

any note or advance deemed to not be fully collectible based upon an estimate of the crop value or the fair value of the security for the note or advance. If crop prices or the fair value of the underlying security declines, the Company may be unable to fully recoup its note or advance receivable and the estimated losses would rise in the current period, potentially to the extent of the total note or advance receivable.

Allowance for Doubtful Accounts

The Company maintains allowances for doubtful accounts for estimated losses resulting from the inability of its customers to make required payments. The allowance for doubtful accounts is based on review of the overall condition of accounts receivable balances and review of significant past due accounts. If the financial condition of the Company's customers were to deteriorate, resulting in an impairment of their ability to make payments, additional allowances may be required. Bad debt losses are partially mitigated due to low risks related to the fact that the Company's customers are predominantly large financially sound national and regional retailers.

Inventories

Inventories are stated at the lower of cost or market. If the cost of the inventories exceeds their expected market value, provisions are recorded currently for the difference between the cost and the market value. These provisions are determined based on specific identification for unusable inventory and an additional reserve, based on historical losses, for inventory currently considered to be useable.

Revenue Recognition

Revenue from product sales is recognized when there is persuasive evidence that an arrangement exists, title has transferred, the price is fixed and determinable, and collectibility is reasonably assured. Allowances are established for estimated uncollectible amounts, product returns, and discounts. If actual future returns and allowances differ from past experience, additional allowances may be required.

Licensing revenue is recognized in accordance with Staff Accounting Bulletin No. 104, *Revenue Recognition (a replacement of SAB 101)*, (SAB 104). Initial license fees are deferred and amortized to revenue over the period of the agreement when a contract exists, the fee is fixed and determinable, and collectibility is reasonably assured. Noncancellable, nonrefundable license fees are recognized over the research and development period of the agreement, as well as the term of any related supply agreement entered into concurrently with the license when the risk associated with commercialization of a product is non-substantive at the outset of the arrangement.

Prior to November 1, 1999, the Company recognized noncancellable, nonrefundable license fees as revenue when received and when all significant contractual obligations of the Company relating to the fees had been met. Effective November 1, 1999, the Company changed its method of accounting for noncancellable, nonrefundable license fees to recognize such fees over the research and development period of the agreement, as well as the term of any related supply agreement entered into concurrently with the license when the risk associated with commercialization of a product is non-substantive at the outset of the arrangement. The Company believes the change in accounting principle is preferable based on guidance provided in SAB 104. In the fiscal year ended October 29, 2000, the Company recorded a charge of $1.9 million related to the cumulative effect of the change in accounting principle. The cumulative effect was initially recorded as deferred revenue and has been recognized as recycled revenue over the research and development period or supply period commitment of the agreement. "Recycled" revenue refers to revenue that had previously been recognized as licensing revenue in the Company's financial statements, but as a result of the Company's adoption of SAB 104, was reversed through a cumulative effect of a change in accounting in fiscal year 2000 and has been recognized as revenue over the research and development period and/or the supply period commitment of the agreement, whichever is longer.

In July 2005, the Company amended its supply agreement with Alcon, Inc. ("Alcon") to change the expiration date of the agreement from November 1, 2012 to May 28, 2006. In accordance with SAB 104, the entire amount of the deferred revenue of $638,000 as of May 29, 2005, was recognized as "recycled" revenue during fiscal year 2006.

During the fiscal years ended May 27, 2007, May 28, 2006 and May 29, 2005 $0, $638,000, and $88,000, respectively, of the related deferred revenue was recognized as "recycled" revenue. As of May 27, 2007 and May 28, 2006, deferred revenue associated with the change in accounting principles described above is zero.

Contract revenue for research and development (R&D) is recorded as earned, based on the performance requirements of the contract. Non-refundable contract fees for which no further performance obligations exist, and there is no continuing involvement by the Company, are recognized on the earlier of when the payments are received or when collection is assured.

Goodwill and Other Intangible Asset Impairment

The Company is required to evaluate its goodwill and indefinite lived intangible assets for impairment annually. This evaluation incorporates a variety of estimates including the fair value of the Company's operating segments. If the carrying value of an operating segment's assets exceeds the estimated fair value, the Company would likely be required to record an impairment loss, possibly for the entire carrying balance of goodwill and intangible assets. To date, no impairment losses have been incurred.

Income Taxes

The Company accounts for income taxes in accordance with SFAS No. 109, "*Accounting for Income Taxes,*" which requires that deferred tax assets and liabilities be recognized using enacted tax rates for the effect of temporary differences between the book and tax bases of recorded assets and liabilities. SFAS No. 109 also requires that deferred tax assets be reduced by a valuation allowance if it is more likely than not that some or all of the deferred tax assets will not be realized. The Company evaluates quarterly the realizability of its deferred tax assets by assessing the valuation allowance and, if necessary, adjusts the amount of such allowance. The factors used to assess the likelihood of realization include the Company's forecast of future taxable income and available tax planning strategies that could be implemented to realize the net deferred tax assets. Due to the Company's limited tax basis earnings history, the net deferred tax asset at May 27, 2007 has been fully offset by a valuation allowance.

Stock-Based Compensation

On May 29, 2006, the Company adopted SFAS 123R, which is a revision of SFAS No. 123 "Accounting for Stock-Based Compensation", and supersedes APB No. 25, "Accounting for Stock Issued to Employees" ("APB 25"). Among other items, SFAS 123R requires companies to record compensation expense for stock-based awards issued to employees and directors in exchange for services provided. The amount of the compensation expense is based on the estimated fair value of the awards on their grant dates and is recognized over the required service periods. The Company's stock-based awards include stock option grants and restricted stock unit awards (RSUs).

Prior to the adoption of SFAS 123R, the Company applied the intrinsic value method set forth in APB 25 to calculate the compensation expense for stock-based awards. The Company has historically set the exercise price for its stock options equal to the market value on the grant date. As a result, the options had no intrinsic value on their grant dates, and therefore the Company did not record any compensation expense unless the terms of the stock options were subsequently modified. For RSUs, the calculation of compensation expense under APB 25 and SFAS 123R is similar except for the accounting treatment for forfeitures as discussed below.

The Company adopted SFAS 123R using the modified prospective transition method, which requires the application of the accounting standard to (i) all stock-based awards issued on or after May 29, 2006 and (ii) any outstanding stock-based awards that were issued but not vested as of May 29, 2006. Accordingly, the Company's consolidated financial statements as of May 28, 2006 and May 29, 2005, and for the fiscal years then-ended, were accounted for under the provisions of APB 25.

The estimated fair value for stock options, which determines the Company's calculation of compensation expense, is based on the Black-Scholes pricing model. Upon the adoption of SFAS 123R, the Company changed its method of calculating and recognizing the fair value of stock-based compensation arrangements to the straight-line, single-option method. Compensation expense for all stock option and restricted stock awards granted prior to May 29, 2006 will continue to be recognized using the straight-line, multiple-option method. In addition, SFAS 123R requires the estimation of the expected forfeitures of stock-based awards at the time of grant. As a result, the Company uses historical data to estimate pre-vesting forfeitures and records stock-based compensation expense only for those awards that are expected to vest and revises those estimates in subsequent periods if the actual forfeitures differ from the prior

estimates. In the pro-forma information required under SFAS 123R for periods prior to May 29, 2006, the Company accounted for forfeitures as they occurred.

Recent Accounting Pronouncements

Fair Value Measurements

In September 2006, the FASB issued SFAS No. 157, "Fair Value Measurements" ("SFAS 157"). SFAS 157 defines fair value, establishes a framework for measuring fair value and expands disclosure of fair value measurements. SFAS 157 applies under other accounting pronouncements that require or permit fair value measurements and accordingly, does not require any new fair value measurements. SFAS 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007. The Company has not determined the impact of the adoption of SFAS 157 on its consolidated financial statements.

Accounting for Uncertainty in Income Taxes

In June 2006, the Financial Accounting Standards Board ("FASB") issued FASB Interpretation No. 48, *Accounting for Uncertainty in Income Taxes — an Interpretation of FASB Statement No. 109* ("FIN No. 48"), which clarifies the accounting for uncertainty in income taxes recognized in an enterprise's financial statements in accordance with FASB Statement No. 109, *Accounting for Income Taxes*. FIN No. 48 prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. FIN No. 48 also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure, and transition and defines the criteria that must be met for the benefits of a tax position to be recognized. The provisions of FIN No. 48 will be effective for the Company commencing at the start of fiscal 2008, May 28, 2007. The Company is currently evaluating the impact of adopting FIN No. 48 on its consolidated financial statements, however, the Company does not expect the adoption of FIN No. 48 to have a material impact on the Company's consolidated financial statements.

Results of Operations

Fiscal Year Ended May 27, 2007 Compared to Fiscal Year Ended May 28, 2006

Revenues (in thousands):

	Fiscal Year ended May 27, 2007	Fiscal Year ended May 28, 2006	Change
Apio Value Added	$ 154,744	$ 136,141	14%
Apio Tech	1,730	685	153%
Technology Subtotal	156,474	136,826	14%
Apio Trading	49,706	57,990	(14%)
Total Apio	206,180	194,816	6%
Landec Ag	2,831	34,096	(92%)
Corporate	1,487	3,041	(51%)
Total Revenues	$ 210,498	$ 231,953	(9%)

Apio Value Added

Apio's value-added revenues consist of revenues generated from the sale of specialty packaged fresh-cut and whole value-added processed vegetable products that are washed and packaged in our proprietary packaging and sold under Apio's Eat Smart brand and various private labels and from service revenues from Apio Cooling LP which is now combined with value-added.

The increase in Apio’s value-added revenues for the fiscal year ended May 27, 2007 compared to the same period last year is due to increased product offerings, increased sales to existing customers and the addition of new customers. Specifically, sales of Apio’s value-added 12-ounce specialty packaged retail product line grew 18% and sales of Apio’s value-added vegetable tray products also grew 18% during the fiscal year ended May 27, 2007 compared to the same period last year. Overall value-added sales volume increased 15% during the fiscal year ended May 27, 2007 compared to the same period last year.

Apio Tech

Apio Tech consists of Apio's packaging technology business using its BreatheWay membrane technology. The first commercial application included in Apio Tech is the banana packaging technology. A large majority of the revenues currently generated by Apio Tech are revenues derived from our banana packaging program with Chiquita.

The increase in Apio Tech revenues for the fiscal year ended May 27, 2007 compared to the same period last year was not material to consolidated Landec revenues.

Apio Trading

Apio trading revenues consist of revenues generated primarily from the purchase and sale of whole commodity fruit and vegetable products to Asia through Apio's export company, Cal-Ex and from the purchase and sale of whole commodity fruit and vegetable products domestically. The export portion of trading revenues for fiscal year 2007 was $46.4 million or 93% of total trading revenues.

The decrease in revenues in Apio's trading business for the fiscal year ended May 27, 2007 compared to the same period last year was primarily due to planned decreases in the domestic buy/sell commodity sales of 57%. Overall trading sales volumes were lower by 27% for the fiscal year ended May 27, 2007 compared to the prior year. In addition, export revenues decreased 8% due to lower sales volumes. The decrease in sales volumes was partially offset by higher average sales prices due to the scarcity of product during certain months of the year.

Landec Ag

Landec Ag revenues have historically consisted of revenues generated from the sale of hybrid seed corn to farmers under the Fielder's Choice Direct brand and from the sale of hybrid seed corn and soybeans under the Heartland Hybrids® brand (these brands, collectively FCD, and the related assets were sold to ASI on December 1, 2006, see Note 2 of Notes to Consolidated Financial Statements) and from the sale of Intellicoat coated corn and soybean seeds to farmers and seed companies. Prior to the sale of FCD, virtually all of Landec Ag's revenues were generated during the Company's third and fourth quarters. As a result of the technology licensing agreement with Monsanto, Landec Ag license fee revenues will be recognized evenly each quarter for a period of five years.

The decrease in revenues at Landec Ag during the fiscal year ended May 27, 2007 compared to the same period last year was primarily due to the sale of FCD to ASI, partially offset by $2.7 million in license fee revenues from the Intellicoat license agreement with Monsanto.

Corporate

Corporate revenues consist of revenues generated from partnering with others under research and development agreements and supply agreements and from fees for licensing our proprietary Intelimer technology to others and from the corresponding royalties from these license agreements.

The decrease in Corporate revenues for the fiscal year ended May 27, 2007 compared to the same period of the prior year resulted from certain nonrecurring licensing revenues recorded in the prior year and was not material to consolidated Landec revenues.

Gross Profit (in thousands):

	Fiscal Year ended May 27, 2007	Fiscal Year ended May 28, 2006	Change
Apio Value Added	$ 23,426	$ 23,022	2%
Apio Tech	1,639	619	165%
Technology Subtotal	25,065	23,641	6%
Apio Trading	3,187	3,212	(1%)
Total Apio	28,252	26,853	5%
Landec Ag	2,647	10,439	(75%)
Corporate	1,487	2,752	(46%)
Total Gross Profit	$ 32,386	$ 40,044	(19%)

General

There are numerous factors that can influence gross profit including product mix, customer mix, manufacturing costs, volume, sale discounts and charges for excess or obsolete inventory, to name a few. Many of these factors influence or are interrelated with other factors. Therefore, it is difficult to precisely quantify the impact of each item individually. The Company includes in cost of sales all of the costs related to the sale of products in accordance with U.S. generally accepted accounting principles. These costs include the following: raw materials (including produce, seeds and packaging), direct labor, overhead (including indirect labor, depreciation, and facility related costs) and shipping and shipping related costs. The following discussion surrounding gross profit includes management's best estimates of the reasons for the changes for the fiscal year ended May 27, 2007 compared to the same period last year as outlined in the table above.

Apio Value-Added

The increase in gross profit for Apio's value-added specialty packaged vegetable business for the fiscal year ended May 27, 2007 compared to the same period last year was due to increased revenues, a more profitable mix of products sold and improved operational efficiencies. The more profitable mix of products sold and improved operational efficiencies were almost completely offset by the increased costs associated with weather related shortages of contracted product during several periods of fiscal 2007. These shortages required Apio to procure supplemental product on the open market at costs significantly above contracted prices and resulted in sales volume decreases and labor cost increases.

Apio Tech

The increase in gross profit for Apio Tech for the fiscal year ended May 27, 2007 compared to the same period last year was primarily due to the revenues received from our licensing agreement with Chiquita and from research and development contracts with other third parties.

Apio Trading

Apio's trading business is a buy/sell business that realizes a commission-based margin in the 4-6% range. The decrease in gross profit during the fiscal year ended May 27, 2007 compared to the prior fiscal year was primarily due to the reduction in revenues which was almost completely offset by a shift to higher margin export products from lower margin domestic commodity products.

Landec Ag

The decrease in gross profit for Landec Ag for the fiscal year ended May 27, 2007 compared to the same periods last year was due to the sale of FCD to ASI and the consequent loss of product sales and gross profit normally recorded during the second half of our fiscal year (see Note 2 of Notes to Consolidated Financial Statements). The decrease in Landec Ag gross profit was partially offset by $2.7 million of gross profit from the Intellicoat license agreement with Monsanto.

Corporate

The decrease in gross profit for Corporate for the fiscal year ended May 27, 2007 compared to the prior year was primarily due to the Aesthetic Sciences' licensing revenues and gross profit recorded in the prior year.

Operating Expenses (in thousands):

	Fiscal Year ended May 27, 2007	Fiscal Year ended May 28, 2006	Change
Research and Development:			
Apio	$ 1,169	$ 1,108	6%
Landec Ag	266	470	(43%)
Corporate	1,639	1,464	(12%)
Total R&D	$ 3,074	$ 3,042	1%
Selling, General and Administrative:			
Apio	$ 12,667	$ 13,633	(7%)
Landec Ag	(17,302)	9,616	(280%)
Corporate	3,582	4,730	(24%)
Total S,G&A	$ (1,053)	$ 27,979	(104%)

Research and Development

Landec's research and development expenses consist primarily of expenses involved in product development and commercialization initiatives. Research and development efforts at Apio are focused on the Company's proprietary BreatheWay membranes used for packaging produce, with recent focus on extending the shelf life of bananas and other shelf-life sensitive vegetables and fruit. At Landec Ag, the research and development efforts are focused on the Company's proprietary Intellicoat coatings for seeds, primarily corn seed. Beginning December 1, 2006, all of the operating costs and expense of Landec Ag are being paid for by Monsanto in accordance with the technology license and supply agreement (see Note 2 of Notes to Consolidated Financial Statements). At Corporate, the research and development efforts are primarily focused on uses for the proprietary Intelimer polymers outside of food and agriculture.

The increase in research and development expenses for the fiscal year ended May 27, 2007 compared to the same period last year was not material.

Selling, General and Administrative

Selling, general and administrative expenses consist primarily of sales and marketing expenses associated with Landec's product sales and services, business development expenses and staff and administrative expenses.

The decrease in selling, general and administrative expenses for the fiscal year ended May 27, 2007 compared to the same period last year was due to (1) the income realized from the sale of FCD to ASI (see Note 2 of Notes to Consolidated Financial Statements), (2) one-time new packaging design and marketing related costs that were incurred at Apio during the first quarter of fiscal year 2006 and (3) the recording of the net proceeds of $1.5 million from an insurance settlement (see Note 6 of Notes to Consolidated Financial Statements) to Corporate selling, general and administrative expenses during the first six months of fiscal year 2007.

Other (in thousands):

	Fiscal Year ended May 27, 2007	Fiscal Year ended May 28, 2006	Change
Interest Income	$ 1,945	$ 633	207%
Interest Expense	(251)	(452)	(44%)
Minority Interest Expense	(412)	(529)	(22%)
Other Expenses	(2)	(24)	(92%)
Total Other Income (Exp.)	$ 1,280	$ (372)	444%
Income taxes	$ (2,456)	$ 0	N/M

Interest Income

The increase in interest income for the fiscal year ended May 27, 2007 compared to the prior year was primarily due to the increase in cash available for investing and higher average interest rates on those investments.

Interest Expense

The decrease in interest expense during the fiscal year ended May 27, 2007 compared to the prior year was due to the Company's reduction of debt.

Minority Interest Expense

The minority interest expense consists of the minority interest associated with the limited partners' equity interest in the net income of Apio Cooling, LP.

The decrease in the minority interest expense in fiscal year 2007 compared to fiscal year 2006 was due to non-recurring gains for Apio Cooling during the first quarter of fiscal year 2006.

Other Expenses

Other consists of non-operating income and expenses.

Income Taxes

The increase in the income tax expense in fiscal year 2007 is due to the income realized from the sale of FCD which resulted in the Company recording a tax provision of $2.5 million for state income taxes and federal AMT.

Fiscal Year Ended May 28, 2006 Compared to Fiscal Year Ended May 29, 2005

Revenues (in thousands):

	Fiscal Year ended May 28, 2006	**Fiscal Year ended May 29, 2005**	**Change**
Apio Value Added	$ 136,141	$ 120,445	13%
Apio Tech	685	52	1217%
Technology Subtotal	136,826	120,497	14%

Apio Trading		57,990		58,660	(1%)
Total Apio		194,816		179,157	9%
Landec Ag		34,096		25,648	33%
Corporate		3,041		425	616%
Total Revenues	$	231,953	$	205,230	13%

Apio Value Added

Apio's value-added revenues consist of revenues generated from the sale of specialty packaged fresh-cut and whole value-added processed vegetable products that are washed and packaged in our proprietary packaging and sold under Apio's Eat Smart brand and various private labels and from service revenues from Apio Cooling LP which is now combined with value-added.

The increase in Apio's value-added revenues for the fiscal year ended May 28, 2006 compared to the same period last year is due to increased product offerings, increased sales to existing customers, the addition of new customers and product mix changes to higher priced products. Specifically, sales of Apio's value-added 12-ounce specialty packaged retail product line grew 16% and sales of Apio's value-added vegetable tray products grew 22% during the fiscal year ended May 28, 2006 compared to the same period last year. Overall value-added sales volume increased 10% during the fiscal year ended May 28, 2006 compared to the same period last year.

Apio Tech

Apio Tech consists of Apio's packaging technology business using its BreatheWay™ membrane technology. The first commercial application included in Apio Tech is the banana packaging technology. Current revenues generated from Apio Tech are primarily from the banana program with Chiquita.

The increase in Apio Tech revenues for the fiscal year ended May 28, 2006 compared to the same period last year was not material to consolidated Landec revenues.

Apio Trading

Apio trading revenues consist of revenues generated from the purchase and sale of primarily whole commodity fruit and vegetable products to Asia through Apio's export company, Cal-Ex and from the purchase and sale of whole commodity fruit and vegetable products domestically to Wal-Mart. The export portion of trading revenues for fiscal year 2006 was $50.3 million or 87% of total trading revenues.

The decrease in revenues in Apio's trading business for the fiscal year ended May 28, 2006 compared to the same period last year was primarily due to a 23% decrease in the domestic buy/sell commodity sales to Wal-Mart. Overall trading sales volumes were lower by 2% for the fiscal year ended May 28, 2006 compared to the same period last year. The decrease in volumes was partially offset by higher average sales prices due to the scarcity of product during certain months of the year.

Landec Ag

Landec Ag revenues consist of revenues generated from the sale of hybrid seed corn to farmers under the Fielder's Choice Directâ and Heartland Hybrids® brands and from the sale of Intellicoat coated corn and soybean seeds to farmers and seed companies. For the fiscal years ended May 28, 2006 and May 29, 2005, over 95% of Landec Ag's revenues were from the sale of uncoated hybrid seed corn.

The increase in revenues at Landec Ag during the fiscal year ended May 28, 2006 compared to the same period last year was primarily due to sales under the Heartland Hybrids brand which was acquired on August 29, 2005.

Corporate

Corporate revenues consist of revenues generated from partnering with others under research and development agreements and supply agreements and from fees for licensing our proprietary Intelimer technology to others and from the corresponding royalties from these license agreements.

The increase in Corporate revenues for the fiscal year ended May 28, 2006 compared to the same period of the prior year was primarily due to (1) $1.56 million in revenues received from the license of our Intelimer technology in a specific field to a medical device company in December 2005, (2) $300,000 in licensing fees and research and development revenues from the license of our Intelimer technology in specific fields to Air Products in March 2006 and (3) the recognition of the remaining $550,000 of deferred revenue associated with the Alcon license agreement through the revised agreement termination date of May 28, 2006.

Gross Profit (in thousands):

	Fiscal Year ended May 28, 2006	Fiscal Year ended May 29, 2005	Change
Apio Value Added	$ 23,022	$ 19,062	21%
Apio Tech	619	15	4027%
Technology Subtotal	23,641	19,077	24%
Apio Trading	3,212	3,118	3%
Total Apio	26,853	22,195	21%
Landec Ag	10,439	9,448	10%
Corporate	2,752	329	736%
Total Gross Profit	$ 40,044	$ 31,972	25%

General

There are numerous factors that can influence gross profit including product mix, customer mix, manufacturing costs, volume, sale discounts and charges for excess or obsolete inventory, to name a few. Many of these factors influence or are interrelated with other factors. Therefore, it is difficult to precisely quantify the impact of each item individually. The Company includes in cost of sales all the costs related to the sale of products in accordance with generally accepted accounting principles. These costs include the following: raw materials (including produce, seeds and packaging), direct labor, overhead (including indirect labor, depreciation, and facility related costs) and shipping and shipping related costs. The following discussion surrounding gross profit includes management’s best estimates of the reasons for the changes for the fiscal year ended May 28, 2006 compared to the same period last year as outlined in the table above.

Apio Value-Added

The increase in gross profit for Apio’s value-added specialty packaged vegetable business for the fiscal year ended May 28, 2006 compared to the same period last year was due to (1) the increase in value-added sales which increased 13% during fiscal year 2006, (2) product mix changes to higher margin products and (3) improved operational efficiencies driven largely by improved raw material quality during fiscal year 2006 compared to the prior fiscal year.

Apio Tech

The increase in gross profit for Apio Tech for the fiscal year ended May 28, 2006 compared to the same period last year was primarily due to the revenues received from our licensing agreement with Chiquita.

Apio Trading

Apio’s trading business is a buy/sell business that realizes a commission-based margin in the 4-6% range. The increase in gross profit during the fiscal year ended May 28, 2006 compared to the prior fiscal year was primarily due to product mix changes to higher margin products which more than offset the reduction in revenues.

Landec Ag

The increase in gross profit for Landec Ag for the fiscal year ended May 28, 2006 compared to the same period last year was due to the increase in revenues as a result of the acquisition of Heartland Hybrids in August 2005, partially offset by higher royalty fees on corn seed hybrids with traits, such as genetics and certain chemicals, resulting in lower gross profit as a percentage of sales in fiscal year 2006 compared to the same period last year.

Corporate

The increase in gross profit for Corporate for the fiscal year ended May 28, 2006 compared to the same period last year was primarily due to (1) $1.56 million in revenues received from the license of our Intelimer technology in a specific field to a medical device company in December 2005, (2) $300,000 in licensing fees and research and development revenues from the license of our Intelimer technology in specific fields to Air Products in March 2006 and (3) the recognition of the remaining $550,000 of deferred revenue associated with the Alcon license agreement through the revised agreement termination date of May 28, 2006.

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Operating Expenses (in thousands):

		Fiscal Year ended May 28, 2006		***Fiscal Year ended May 29, 2005***	***Change***
Research and Development:					
Apio	$	1,108	$	831	33%
Landec Ag		470		647	(27%)
Corporate		1,464		1,065	37%
Total R&D	$	3,042	$	2,543	20%
Selling, General and Administrative:					
Apio	$	13,633	$	12,354	10%
Landec Ag		9,616		7,857	22%
Corporate		4,730		3,201	48%
Total S,G&A	$	27,979	$	23,412	20%

Research and Development

Landec’s research and development expenses consist primarily of expenses involved in product development and commercalization initiatives. Research and development efforts at Apio are focused on the Company’s proprietary BreatheWay membranes used for packaging produce, with recent focus on extending the shelf life of bananas and other shelf-life sensitive vegetables and fruit. At Landec Ag, the research and development efforts are focused on the Company’s proprietary Intellicoat coatings for seeds, primarily corn seed. At Corporate, the research and development efforts are primarily focused on uses for the proprietary Intelimer polymers outside of food and agriculture.

The increase in research and development expenses for the fiscal year ended May 28, 2006 compared to the same period last year was due to increased efforts expended at Apio Tech to expand its initiatives to programs beyond just bananas and increased expenses at Corporate to support new collaborations, including the addition of Landec’s COO, Dr. David Taft, who was the COO of Apio in fiscal year 2005.

Selling, General and Administrative

Selling, general and administrative expenses consist primarily of sales and marketing expenses associated with Landec’s product sales and services, business development expenses and staff and administrative expenses.

The increase in selling, general and administrative expenses for the fiscal year ended May 28, 2006 compared to the same period last year was primarily due to (1) selling, general and administrative expenses of $2.0 million at Heartland Hybrids, (2) planned increases in selling and marketing expenses at Apio and Landec Ag to generate

increases in revenues, (3) an increase in general and administrative expenses at Corporate for business development consulting fees and legal fees, (4) the accrual of bonuses for exceeding our fiscal year 2006 internal plan and (5) in fiscal year 2005 a $713,000 gain on the sale of land at Apio was netted against selling, general and administrative expenses.

Other (in thousands):

	Fiscal Year ended May 28, 2006	Fiscal Year ended May 29, 2005	Change
Interest Income	$ 633	$ 214	196%
Interest Expense	(452)	(414)	9%
Minority Interest Expense	(529)	(411)	29%
Other Expenses	(24)	(4)	500%
Total Other Expense	$ (372)	$ (615)	(40%)

Interest Income

The increase in interest income for the fiscal year ended May 28, 2006 compared to the same period last year was primarily due to the increase in cash available for investing and higher average interest rates on those investments.

Interest Expense

The increase in interest expense during the fiscal year ended May 28, 2006 compared to the same period last year was due to higher average interest rates on the Company's debt.

Minority Interest Expense

The minority interest expense consists of the minority interest associated with the limited partners' equity interest in the net income of Apio Cooling, LP.

The increase in the minority interest expense in fiscal year 2006 compared to fiscal year 2005 was due to higher net income for Apio Cooling in fiscal year 2006 compared to fiscal year 2005.

Other Expenses

Other consists of non-operating income and expenses.

Liquidity and Capital Resources

As of May 27, 2007, the Company had cash and cash equivalents of $62.6 million, a net increase of $42.1 million from $20.5 million at May 28, 2006 including Landec Ag's cash of $5.3 million as of May 28, 2006.

Cash Flow from Operating Activities

Landec used $2.1 million of cash flow in operating activities during the fiscal year ended May 27, 2007 compared to generating $10.9 million from operating activities for the fiscal year ended May 28, 2006. The primary sources of cash during fiscal year 2007 were from fiscal year 2007 net income and non-cash related income/expenses, such as the income from the sale of FCD and depreciation, of $8.5 million and an increase in deferred revenue of $2.6 million due to the annual license payment received in accordance with the license agreement with Monsanto (see Note 2 of Notes to Consolidated Financial Statements). The primary uses of cash in operating activities during fiscal year 2007 were from an $8.7 million increase in inventory, primarily due to the purchase of seed corn inventory by Landec Ag of $7.9 million prior to the sale of FCD on December 1, 2006 and a decrease in accounts payable of $2.9 million of which $4.8 million was from Landec Ag which was primarily related to royalty payments from fiscal year 2006 sales prior to the sale of FCD.

Cash Flow from Investing Activities

Net cash provided by investing activities for the year ended May 27, 2007 was $42 million compared to the use of $5.5 million for the same period last year. The primary source of cash from investing activities during fiscal year 2007 was from $49.4 million of proceeds, net of direct transaction expenses, from the sale of FCD. The primary uses of cash from investing activities during fiscal year 2007 were from the purchase of $6.8 million of property, plant and equipment primarily for the further expansion and automation of Apio's value-added facility.

Cash Flow from Financing Activities

Net cash provided by financing activities for the fiscal year ended May 27, 2007 was $2.1 million compared to $2.3 million for the same period last year. The cash provided by financing activities during fiscal year 2007 was primarily due to net borrowings under Landec Ag's line of credit of $9.3 million primarily for the purchase of seed corn (the line of credit was assumed by Monsanto in the sale of FCD and was immediately paid in full) and $2.7 million of cash received from employees exercising their stock options. The cash used from financing activities during fiscal year 2007 was primarily used to buy back Landec Ag's subsidiary options and stock for $7.4 million and to pay off all of Apio's long-term bank debt totaling $2.0 million.

Capital Expenditures

During the fiscal year ended May 27, 2007, Landec expanded Apio's value added processing facility and purchased vegetable processing equipment to support the further automation of Apio's value added processing facility. These expenditures represented the majority of the $6.8 million of capital expenditures.

Debt

On November 1, 2005, Apio amended its revolving line of credit with Wells Fargo Bank N.A. extending the term of the line to August 31, 2007. In addition, the line was reduced from $10.0 million to $7.0 million and outstanding amounts under the line of credit now bear interest at either the prime rate less 0.25% or the LIBOR adjustable rate plus 1.75% (7.07% at May 27, 2007). The revolving line of credit with Wells Fargo contains certain restrictive covenants, which require Apio to meet certain financial tests, including minimum levels of net income, maximum leverage ratio, minimum net worth and maximum capital expenditures. Landec has pledged substantially all of the assets of Apio to secure the line of credit with Wells Fargo. At May 27, 2007, no amounts were outstanding under the revolving line of credit. Apio has been in compliance with all loan covenants since the inception of this loan.

On August 29, 2006, Landec Ag amended and restated its revolving line of credit with Old National Bank which increased the line from $7.5 million to $10 million. In conjunction with the sale of FCD to ASI on December 1, 2006 (see Note 2 of Notes to Consolidated Financial Statements), Landec Ag's line of credit was paid in full by ASI and subsequently terminated.

Contractual Obligations

The Company's material contractual obligations for the next five years and thereafter as of May 27, 2007, are as follows (in thousands):

		Due in Fiscal Year Ended May					
Obligation	Total	2008	2009	2010	2011	2012	Thereafter
Capital Leases	$ 28	28	—	—	—	—	—
Operating Leases	1,096	535	352	180	29	—	—

Licensing Obligation	500	100	100	100	100	100	—
Purchase Commitments	1,862	1,862	—	—	—	—	—
Total	$ 3,486	$ 2,525	$ 452	$ 280	$ 129	$ 100	$ —

Landec is not a party to any agreements with, or commitments to, any special purpose entities that would constitute material off-balance sheet financing other than the operating lease commitments listed above.

Landec's future capital requirements will depend on numerous factors, including the progress of its research and development programs; the continued development of marketing, sales and distribution capabilities; the ability of Landec to establish and maintain new collaborative and licensing arrangements; any decision to pursue additional acquisition opportunities; weather conditions that can affect the supply and price of produce, the timing and amount, if any, of payments received under licensing and research and development agreements; the costs involved in preparing, filing, prosecuting, defending and enforcing intellectual property rights; the ability to comply with regulatory requirements; the emergence of competitive technology and market forces; the effectiveness of product commercialization activities and arrangements; and other factors. If Landec's currently available funds, together with the internally generated cash flow from operations are not sufficient to satisfy its capital needs, Landec would be required to seek additional funding through other arrangements with collaborative partners, additional bank borrowings and public or private sales of its securities. There can be no assurance that additional funds, if required, will be available to Landec on favorable terms if at all.

Landec believes that its debt facilities, cash from operations, along with existing cash, cash equivalents and existing borrowing capacities will be sufficient to finance its operational and capital requirements for the foreseeable future.

Item 7A. ***Quantitative and Qualitative Disclosures about Market Risk***

The following table presents information about the Company's debt obligations and derivative financial instruments that are sensitive to changes in interest rates. The table presents principal amounts and related weighted average interest rates by fiscal year of expected maturity for the Company's debt obligations. The carrying value of the Company's debt obligations approximates the fair value of the debt obligations as of May 27, 2007.

Liabilities (in 000's)	2008	2009	2010	2011	2012	There-after	Total
Lines of Credit	$ —	$ —	$ —	$ —	$ —	$ —	$ —
Avg. Int. Rate							
Long term debt, including current portion							
Fixed Rate	$ 28	$ —	$ —	$ —	$ —	$ —	$ 28
Avg. Int. Rate	5.90%						5.90%

Item 8. ***Financial Statements and Supplementary Data***

See Item 15 of Part IV of this report.

Item 9. ***Changes in and Disagreements with Accountants on Accounting and Financial Disclosure***

Not applicable.

Item 9A. ***Controls and Procedures***

Evaluation of Disclosure Controls and Procedures

Our management evaluated, with participation of our Chief Executive Officer and our Chief Financial Officer, the effectiveness of our disclosure controls and procedures as of the end of the period covered by this Annual Report on Form 10-K. Based on this evaluation, our Chief Executive Officer and our Chief Financial Officer have concluded that our disclosure controls and procedures are effective in ensuring that information required to be disclosed in reports filed under the Exchange Act is recorded, processed, summarized and reported within the time periods specified by the Securities and Exchange Commission, and to provide reasonable assurance that information required to be disclosed by the Company in such reports is accumulated and communicated to the Company's management, including its Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure.

Changes in Internal Controls over Financial Reporting

There were no changes in our internal controls over financial reporting during the quarter ended May 27, 2007 that have materially affected, or are reasonably likely to materially affect, our internal controls over financial reporting.

Management's Report on Internal Control over Financial Reporting

Our management is responsible for establishing and maintaining adequate internal control over financial reporting (as defined in Rule 13a-15(f) under the Securities Exchange Act of 1934, as amended). Our management assessed the effectiveness of our internal control over financial reporting as of May 27, 2007. In making this assessment, our management used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission ("COSO") in Internal Control - Integrated Framework. Our management has concluded that, as of May 27, 2007, our internal control over financial reporting was effective to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. Our independent registered public accounting firm, Ernst & Young LLP, have issued an audit report on our assessment of our internal control over financial reporting, which is included herein.

Our management, including our Chief Executive Officer and Chief Financial Officer, does not expect that our disclosure controls and procedures or our internal control over financial reporting will prevent all error and all fraud. A control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. Further, the design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within the Company have been detected.

Report of Independent Registered Public Accounting Firm

The Board of Directors and Shareholders of Landec Corporation

We have audited management's assessment, included in the accompanying Management Report on Internal Controls over Financial Reporting, that Landec Corporation maintained effective internal control over financial reporting as of May 27, 2007, based on criteria established in Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (the COSO criteria). Landec Corporation's management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting. Our responsibility is to express an opinion on management's

assessment and an opinion on the effectiveness of the company's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, evaluating management's assessment, testing and evaluating the design and operating effectiveness of internal control, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, management's assessment that Landec Corporation maintained effective internal control over financial reporting as of May 27, 2007, is fairly stated, in all material respects, based on the COSO criteria. Also, in our opinion, Landec Corporation maintained, in all material respects, effective internal control over financial reporting as of May 27, 2007, based on the COSO criteria.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets of Landec Corporation and subsidiaries as of May 27, 2007 and May 28, 2006, and the related statements of income, shareholders' equity, and cash flows for each of the periods ended May 27, 2007, May 28, 2006 and May 29, 2005 of Landec Corporation and our report dated July 23, 2007 expressed an unqualified opinion thereon.

Ernst & Young LLP

San Francisco, California

July 23, 2007

Item 9B. ***Other Information***

None

PART III

Item 10. ***Directors and Executive Officers of the Registrant***

This information required by this item will be contained in the Registrant's definitive proxy statement which the Registrant will file with the Commission no later than September 24, 2007 (120 days after the Registrant's fiscal year end covered by this Report) and is incorporated herein by reference.

Item 11. ***Executive Compensation***

This information required by this item will be contained in the Registrant's definitive proxy statement which the Registrant will file with the Commission no later than September 24, 2007 (120 days after the Registrant's fiscal year end covered by this Report) and is incorporated herein by reference.

Item 12. ***Security Ownership of Certain Beneficial Owners and Management***

This information required by this item will be contained in the Registrant's definitive proxy statement which the Registrant will file with the Commission no later than September 24, 2007 (120 days after the Registrant's fiscal year end covered by this Report) and is incorporated herein by reference.

Item 13. ***Certain Relationships and Related Transactions and Director Independence***

This information required by this item will be contained in the Registrant's definitive proxy statement which the Registrant will file with the Commission no later than September 24, 2007 (120 days after the Registrant's fiscal year end covered by this Report) and is incorporated herein by reference.

Item 14. ***Principal Accountant Fees and Services***

This information required by this item will be contained in the Registrant's definitive proxy statement which the Registrant will file with the Commission no later than September 24, 2007 (120 days after the Registrant's fiscal year end covered by this Report) and is incorporated herein by reference.

PART IV

Item 15. ***Exhibits and Financial Statement Schedules***

(a) 1. Consolidated Financial Statements of Landec Corporation

		Page
	Report of Ernst & Young LLP, Independent Registered Public Accounting Firm	44
	Consolidated Balance Sheets at May 27, 2007 and May 28, 2006	45
	Consolidated Statements of Income for the Years Ended May 27, 2007, May 28, 2006 and May 29, 2005	46
	Consolidated Statements of Changes in Shareholders' Equity for the Years Ended May 27, 2007, May 28, 2006 and May 29, 2005	47
	Consolidated Statements of Cash Flows for the Years Ended May 27, 2007, May 28, 2006 and May 29, 2005	48
	Notes to Consolidated Financial Statements	49
2.	All schedules provided for in the applicable accounting regulations of the Securities and Exchange Commission have been omitted since they pertain to items which do not appear in the financial statements of Landec Corporation and its subsidiaries or to items which are not significant or to items as to which the required disclosures have been made elsewhere in the financial statements and supplementary notes and such schedules.	
3.	Index of Exhibits	78
	The exhibits listed in the accompanying Index of Exhibits are filed or incorporated by reference as part of this report.	

REPORT OF ERNST & YOUNG LLP, INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

Board of Directors and Shareholders
Landec Corporation

We have audited the accompanying consolidated balance sheets of Landec Corporation and subsidiaries as of May 27, 2007 and May 28, 2006, and the related consolidated statements of income, shareholders' equity, and cash flows for each of the three years ended May 27, 2007. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Landec Corporation and subsidiaries at May 27, 2007 and May 28, 2006, and the consolidated results of their operations and their cash flows for each of the three years ended May 27, 2007, in conformity with U.S. generally accepted accounting principles.

As discussed in Note 1 to the Consolidated Financial Statements, on May 29, 2006, Landec Corporation adopted Statement of Financial Accounting Standards No. 123R, “Share-Based Payment”.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the effectiveness of Landec Corporation’s internal control over financial reporting as of May 27, 2007, based on criteria established in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated July 23, 2007 expressed an unqualified opinion thereon.

/s/ ERNST & YOUNG LLP

San Francisco, California
July 23, 2007

LANDEC CORPORATION
CONSOLIDATED BALANCE SHEETS
(in thousands, except share and per share amounts)

	May 27, 2007	May 28, 2006
ASSETS		
Current assets:		
Cash and cash equivalents	$ 62,556	$ 15,164
Accounts receivable, less allowance for doubtful accounts of $206 and $195 at May 27, 2007 and May 28, 2006, respectively	17,631	15,288
Accounts receivable, related party	554	561
Inventories, net	6,800	6,134
Notes and advances receivable, net	282	376
Notes receivable, related party	¾	14
Prepaid expenses and other current assets	1,316	1,237
Assets held for sale (Note 2)	¾	31,838
Total current assets	89,139	70,612
Property and equipment, net	20,270	16,882
Goodwill, net	21,402	21,248
Trademarks, net	8,228	8,228
Notes receivable	96	631
Other assets	2,233	1,424
Total Assets	$ 141,368	$ 119,025
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	$ 13,705	$ 12,443
Related party payables	175	533
Income taxes payables	458	—
Accrued compensation	3,126	2,764
Other accrued liabilities	1,312	1,968
Deferred revenue	3,491	811
Current maturities of long term debt	28	2,018
Liabilities assumed by buyer of FCD (Note 2)		11,668
Total current liabilities	22,295	32,205
Deferred revenue	7,000	—
Minority interest	1,845	1,771
Total liabilities	31,140	33,976
Shareholders' equity:		
Common stock, $0.001 par value; 50,000,000 shares authorized; 25,891,168 and 24,917,298 shares issued and outstanding at May 27, 2007 and May 28, 2006, respectively	129,560	126,288
Accumulated deficit	(19,332)	(41,239)

Total shareholders' equity		110,228		85,049
Total Liabilities and Shareholders' Equity	$	141,368	$	119,025

See accompanying notes.

LANDEC CORPORATION
CONSOLIDATED STATEMENTS OF INCOME
(in thousands, except per share amounts)

Statement of Operations Data:	**Year Ended May 27, 2007**	**Year Ended May 28, 2006**	**Year Ended May 29, 2005**
Revenues:			
Product sales	$ 201,892	$ 225,404	$ 201,020
Services revenue, related party	3,539	3,725	3,704
License fees	4,013	2,398	88
Research, development and royalty revenues	805	162	185
Royalty revenues, related party	249	264	233
Total revenues	210,498	231,953	205,230
Cost of revenue:			
Cost of product sales	172,251	184,345	164,027
Cost of product sales, related party	3,001	4,559	6,332
Cost of services revenue	2,860	3,005	2,899
Total cost of revenue	178,112	191,909	173,258
Gross profit	32,386	40,044	31,972
Operating costs and expenses:			
Research and development	3,074	3,042	2,543
Selling, general and administrative	21,616	27,979	23,412
Income from sale of FCD (Note 2)	(22,669)	—	—
Total operating costs and expenses	2,021	31,021	25,955
Operating income	30,365	9,023	6,017
Interest income	1,945	633	214
Interest expense	(251)	(452)	(414)
Minority interest expense	(412)	(529)	(411)
Other expense, net	(2)	(24)	(4)
Net income before taxes	$ 31,645	$ 8,651	$ 5,402
Income tax expense	(2,456)	—	—
Net income	$ 29,189	$ 8,651	$ 5,402
Basic net income per share	$ 1.16	$ 0.35	$ 0.23
Diluted net income per share	$ 1.07	$ 0.32	$ 0.21
Shares used in per share computation:			
Basic	25,260	24,553	23,705
Diluted	26,558	25,657	24,614

See accompanying notes.

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LANDEC CORPORATION
CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY
(in thousands, except share and per share amounts)

	Common Stock		Accumulated	Total Shareholders'
	Shares	Amount	Deficit	Equity
Balance at May 30, 2004	23,182,020	$ 116,841	$ (55,292)	$ 61,549
Issuance of common stock at $0.86 to $7.20 per share	904,348	5,109	—	5,109
Net income and comprehensive income	—	—	5,402	5,402
Balance at May 29, 2005	24,086,368	121,950	(49,890)	72,060
Issuance of common stock at $0.86 to $6.75 per share	678,744	3,378	—	3,378
Issuance of common stock for the net assets of Heartland Hybrids	152,186	960	—	960
Net income and comprehensive income	—	—	8,651	8,651
Balance at May 28, 2006	24,917,298	126,288	(41,239)	85,049
Issuance of common stock at $1.66 to $8.86 per share	973,870	2,657	—	2,657
Stock-based compensation	—	615	—	615
Repurchase of subsidiary common stock and options	—	—	(7,282)	(7,282)
Net income and comprehensive income	—	—	29,189	29,189
Balance at May 27, 2007	25,891,168	$ 129,560	$ (19,332)	$ 110,228

See accompanying notes

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LANDEC CORPORATION
CONSOLIDATED STATEMENTS OF CASH FLOWS
(in thousands)

	Year Ended May 27, 2007	Year Ended May 28, 2006	Year Ended May 29, 2005
Cash flows from operating activities:			
Net income	$ 29,189	$ 8,651	$ 5,402
Adjustments to reconcile net income to net cash (used in) provided by operating activities:			
Depreciation and amortization	3,260	3,203	3,467
Gain from sale of FCD (Note 2)	(24,587)	—	—
Stock-based compensation	615	—	—
Net loss (gain) on disposal of property and equipment	43	(120)	149
Minority interest	412	529	414
Investment in unconsolidated business	(481)	(1,311)	—
Changes in assets and liabilities, net of effects from acquisitions:			
Accounts receivable, net	(266)	(1,968)	(532)
Inventories, net	(8,733)	(3,123)	1,310
Issuance of notes and advances receivable	(2,186)	(1,761)	(448)
Collection of notes and advances receivable	2,228	1,882	1,250
Prepaid expenses and other current assets	(268)	431	(515)
Accounts payable	(3,425)	3,685	2,553
Related party payables	(358)	(260)	363
Income taxes payable	458	—	—
Accrued compensation	95	1,396	337
Other accrued liabilities	(658)	(146)	(365)
Deferred revenue	2,600	(223)	(337)
Net cash (used in) provided by operating activities	(2,062)	10,865	13,048
Cash flows from investing activities:			
Purchases of property and equipment	(6,782)	(4,746)	(3,658)
Net proceeds from sale of FCD (Note 2)	49,441	—	—
Acquisition of businesses, net of cash acquired	(1,218)	(3,860)	—
Issuance of notes and advances receivable	(37)	(425)	—
Collection of notes and advances receivable	638	224	408
Proceeds from the sale of property and equipment	—	1,350	22
Purchase of marketable securities	—	(991)	(1,968)
Proceeds from maturities of marketable securities	—	2,959	—
Net cash provided by (used in) investing activities	42,042	(5,489)	(5,196)
Cash flows from financing activities:			
Proceeds from sale of common stock	2,657	3,378	5,109
Proceeds from the exercise of subsidiary options	66	105	50
Repurchase of subsidiary common stock and options	(7,384)	—	—
Net change in other assets	(328)	254	(140)
Borrowings on lines of credit	9,338	14,904	59,441
Payments on lines of credit	—	(14,904)	(64,758)

Payments on long term debt	(1,990)	(1,136)	(1,791)
Proceeds from issuance of long term debt	—	—	1,200
Payments to minority interest .	(302)	(329)	(550)
Net cash provided by (used in) financing activities	2,057	2,272	(1,439)
Net increase in cash and cash equivalents	42,037	7,648	6,413
Cash and cash equivalents at beginning of year (including FCD)	20,519	12,871	6,458
Cash and cash equivalents at end of year (including FCD)	62,556	20,519	12,871
Less: Cash held in assets held for sale	—	(5,355)	(5,445)
Cash and cash equivalents at end of year	$ 62,556	$ 15,164	$ 7,426
Supplemental disclosure of cash flows information:			
Cash paid during the period for interest	$ 179	$ 312	$ 511
Cash paid during the period for income taxes	$ 1,998	$ —	$ 50
Supplemental schedule of noncash operating and investing activities:			
Preferred stock received from investment in unconsolidated business	$ 481	$ 1,311	$ —
Sale of land and equipment for note receivable	$ —	$ 380	$ —

See accompanying notes.

LANDEC CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. Organization, Basis of Presentation, and Summary of Significant Accounting Policies

Organization

Landec Corporation and its subsidiaries ("Landec" or the "Company") design, develop, manufacture, and sell temperature-activated and other specialty polymer products for a variety of food products, agricultural products, and licensed partner applications. The Company sells Intellicoat® coated seed products through its Landec Ag, Inc. ("Landec Ag") subsidiary and specialty packaged fresh-cut vegetables and whole produce to retailers and club stores, primarily in the United States and Asia through its Apio, Inc. ("Apio") subsidiary.

Basis of Presentation

Basis of Consolidation

The consolidated financial statements comprise the accounts of Landec Corporation and its subsidiaries, Apio and Landec Ag. All material inter-company transactions and balances have been eliminated.

Reclassifications

Certain reclassifications have been made to prior year financial statements to conform to the current year presentation. For comparability purposes, the assets of Fielder's Choice Direct ("FCD") and the liabilities assumed by the buyer of FCD have been reclassed as of May 28, 2006 in the accompanying Consolidated Balance Sheets (see Note 2).

Summary of Significant Accounting Policies

Use of Estimates

The preparation of financial statements in conformity with U.S. accounting principles generally accepted requires management to make certain estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported results of operations during the reporting period. Actual results could differ materially from those estimates.

For instance, the carrying value of notes and advances receivable, are impacted by current market prices for the related crops, weather conditions and the fair value of the underlying security obtained by the Company, such as, liens on property and crops. The Company recognizes losses when it estimates that the fair value of the related crops or security is insufficient to cover the advance or note receivable.

Concentrations of Risk

Cash and cash equivalents, trade accounts receivable, grower advances and notes receivable are financial instruments that potentially subject the Company to concentrations of credit risk. Corporate policy limits, among other things, the amount of credit exposure to any one issuer and to any one type of investment, other than securities issued or guaranteed by the U.S. government. The Company routinely assesses the financial strength of customers and growers and, as a consequence, believes that trade receivables, grower advances and notes receivable credit risk exposure is limited. Credit losses for bad debt are provided for in the consolidated financial statements through a charge to operations. A valuation allowance is provided for known and anticipated credit losses. The recorded amounts for these financial instruments approximate their fair value.

Several of the raw materials used to manufacture the Company's products are currently purchased from a single source, including some monomers used to synthesize Intelimer® polymers and substrate materials for the production of Intelimer packaging used on a multitude of Apio value-added products.

During the fiscal year ended May 27, 2007, sales to the Company's top five customers accounted for approximately 50% of total revenue, with the top customers, Costco Wholesale Corporation and Sam's Club from the Food Products Technology segment, accounted for approximately 21% and 10%, respectively, of total revenues. In addition, approximately 22% of the Company's total revenues were derived from product sales to international customers, none of whom individually accounted for more than 5% of total revenues. As of May 27, 2007, Costco Wholesale Corporation and Sam's Club represented approximately 20% and 11%, respectively, of total accounts receivable.

1. Organization, Basis of Presentation, and Summary of Significant Accounting Policies (continued)

During the fiscal year ended May 28, 2006, sales to the Company's top five customers accounted for approximately 46% of total revenue, with the top customers, Costco Wholesale Corporation and Sam's Club from the Food Products Technology segment, accounted for approximately 16% and 10%, respectively, of total revenues. In addition, approximately 22% of the Company's total revenues were derived from product sales to international customers, none of whom individually accounted for more than 6% of total revenues. As of May 28, 2006, Costco Wholesale Corporation and Sam's Club represented approximately 20% and 11%, respectively, of total accounts receivable.

Impairment Of Long-Lived Assets

Long-lived assets are reviewed for impairment whenever events or changes in circumstances indicate that their carrying amounts may not be recoverable. Recoverability of assets is measured by comparison of the carrying amount of the asset to the net undiscounted future cash flow expected to be generated from the asset. If the future undiscounted cash flows are not sufficient to recover the carrying value of the assets, the assets' carrying value is adjusted to fair value.

The Company regularly evaluates its long-lived assets for indicators of possible impairment. To date, no impairment has been recorded.

Financial Instruments

The Company's financial instruments are primarily composed of marketable debt securities, commercial-term trade payables and grower advances, notes receivable and lines of credit, as well as long-term notes receivables and debt instruments. For short-term instruments, the historical carrying amount is a reasonable estimate of fair value. Fair values for long-term financial instruments not readily marketable are estimated based upon discounted future cash flows at prevailing market interest rates. Based on these assumptions, management believes the fair market values of the Company's financial instruments are not materially different from their recorded amounts as of May 27, 2007.

Allowance for Doubtful Accounts

The Company maintains allowances for doubtful accounts for estimated losses resulting from the inability of its customers to make required payments and sales discounts. The allowance for doubtful accounts is based on review of the overall condition of accounts receivable balances and review of significant past due accounts. The changes in the Company's allowances for doubtful accounts are summarized in the following table (in thousands).

	Balance at beginning of period	Additions charged to costs and expenses	Deductions	Balance at end of period
Year ended May 29, 2005				
Allowance for doubtful accounts receivable and notes receivable	$ 458	$ 69	$ (182)	$ 345
Year ended May 28, 2006				
Allowance for doubtful accounts receivable and notes receivable	$ 345	$ 10	$ (135)	$ 220
Year ended May 27, 2007				
Allowance for doubtful accounts receivable and notes receivable	$ 220	$ 64	$ (78)	$ 206

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1. Organization, Basis of Presentation, and Summary of Significant Accounting Policies (continued)

Revenue Recognition

Revenue from product sales is recognized when there is persuasive evidence that an arrangement exists, title has transferred, the price is fixed and determinable, and collectibility is reasonably assured. Allowances are established for estimated uncollectible amounts, product returns, and discounts.

Licensing revenue is recognized in accordance with Staff Accounting Bulletin No. 104, *Revenue Recognition (a replacement of SAB 101),* (SAB 104). Initial license fees are deferred and amortized over the period of the agreement to revenue when a contract exists, the fee is fixed and determinable, and collectibility is reasonably assured. Noncancellable, nonrefundable license fees are recognized over the research and development period of the agreement, as well as the term of any related supply agreement entered into concurrently with the license when the risk associated with commercialization of a product is non-substantive at the outset of the arrangement.

Prior to November 1, 1999, the Company recognized noncancellable, nonrefundable license fees as revenue when received and when all significant contractual obligations of the Company relating to the fees had been met. Effective November 1, 1999, the Company changed its method of accounting for noncancellable, nonrefundable license fees to recognize such fees over the research and development period of the agreement, as well as the term of any related supply agreement entered into concurrently with the license when the risk associated with commercialization of a product is non-substantive at the outset of the arrangement. The Company believes the change in accounting principle is preferable based on guidance provided in SAB 104. In the fiscal year ended October 29, 2000, the Company recorded a charge of $1.9 million related to the cumulative effect of the change in accounting principle. The cumulative effect was initially recorded as deferred revenue and was being recognized as revenue over the research and development period or supply period commitment of the agreement. During the year ended October 29, 2000, the impact of the change in accounting was to increase the net loss by approximately $1.5 million which was comprised of the $1.9 million cumulative effect of the change as described above, net of $374,000 of the related deferred revenue which was recognized as “recycled” revenue during 2000. “Recycled” revenue refers to revenue that had previously been recognized as licensing revenue in the Company’s financial statements, but as a result of the Company’s adoption of SAB 104, was reversed through a cumulative effect of a change in accounting in fiscal year 2000 and is now being recognized as revenue over the research and development period and/or the supply period commitment of the agreement, whichever is longer.

In July 2005, the Company amended its supply agreement with Alcon, Inc. to change the expiration date of the agreement from November 1, 2012 to May 28, 2006. In accordance with SAB 104, the entire amount of the deferred revenue of $638,000 as of May 29, 2005, was recognized as “recycled” revenue during fiscal year 2006.

Contract revenue for research and development (R&D) is recorded as earned, based on the performance requirements of the contract. Non-refundable contract fees for which no further performance obligations exist, and there is no continuing involvement by the Company, are recognized on the earlier of when the payments are received or when collection is assured.

Other Accounting Policies and Disclosures

Cash and Cash Equivalents

The Company records all highly liquid securities with maturities of three months or less from date of purchase as cash equivalents. Cash equivalents consist mainly of short-term commercial paper, money market funds and U.S. Treasuries.

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1. Organization, Basis of Presentation, and Summary of Significant Accounting Policies (continued)

Inventories

Inventories are stated at the lower of cost (using the first-in, first-out method) or market. As of May 27, 2007 and May 28, 2006 inventories consisted of (in thousands):

	May 27, 2007	May 28, 2006
Finished goods	$ 2,273	$ 2,193
Raw materials	4,527	3,764
Work in process		177
Inventories, net	$ 6,800	$ 6,134

If the cost of the inventories exceeds their expected market value, provisions are recorded currently for the difference between the cost and the market value. These provisions are determined based on specific identification for unusable inventory and an additional reserve, based on historical losses, for inventory considered to be useable.

Advertising Expense

Prior to the sale of FCD on December 1, 2006, the Company deferred certain costs related to direct-response advertising of Landec Ag's hybrid corn seeds. Such costs were amortized over periods (less than one year) that correspond to the estimated revenue stream of the advertising activity. Advertising expenditures for Landec Ag and Apio that are not direct-response advertisements are expensed as incurred. The advertising expense for the Company for fiscal years 2007, 2006 and 2005 was $205,000, $1.6 million and $2.2 million, respectively. The amount of deferred advertising included in prepaid expenses and other current assets at May 27, 2007 and May 28, 2006 was zero and $61,000, respectively.

Notes and Advances Receivable

Apio has made advances to produce growers for crop and harvesting costs and to the buyer of the fruit processing facility. Notes and advances receivable related to operating activities are for the sourcing of crops for Apio's business and notes and advances receivable related to investing activities are for financing transactions with third parties. Typically these advances are paid off within the growing season (less than one year) from harvested crops. Advances not fully paid during the current growing season are converted to interest bearing obligations, evidenced by contracts and notes receivable. These notes and advances receivable are secured by perfected liens on land and/or crops and have terms that range from twelve to sixty months. Notes receivable are periodically reviewed (at least quarterly) for collectibility. A reserve is established for any note or advance deemed to not be fully collectible based upon an estimate of the crop value or the fair value of the security for the note or advance.

Related Party Transactions

Apio provides cooling and distributing services for farms in which the Chief Executive Officer of Apio (the "Apio CEO") has a financial interest and purchases produce from those farms. Apio also purchases produce from Beachside Produce LLC (formerly known as Apio Fresh) for sale to third parties. Beachside Produce is owned by a group of entities and persons that supply produce to Apio. One of the owners of Beachside Produce is the Apio CEO. Revenues, cost of product sales and the resulting payable, and the note receivable from advances for ground lease payments, and crop and harvesting costs are classified as related party in the accompanying financial statements as of May 27, 2007 and May 28, 2006 and for the years ended May 27, 2007, May 28, 2006 and May 29, 2005.

Apio leases, for approximately $504,000 on an annual basis, agricultural land that is either owned, controlled or leased by the Apio CEO. Apio, in turn, subleases that land at cost to growers who are obligated to deliver product from that land to Apio for value added products. There is generally no net statement of operations impact to Apio as a result of these leasing activities but Apio creates a guaranteed source of supply for the value added business. Apio has loss exposure on the leasing activity to the extent that it is unable to sublease the land. For the years ended May 27, 2007, May 28, 2006 and May 29, 2005, the Company subleased all of the land leased from the Apio CEO and received sublease income of $504,000, $554,000 and $1.0 million, respectively, which is substantially equal to the amount the Company paid to lease that land for such periods.

1. Organization, Basis of Presentation, and Summary of Significant Accounting Policies (continued)

Apio's domestic commodity vegetable business was sold to Beachside Produce, effective June 30, 2003. The Apio CEO is a 12.5% owner in Beachside Produce. During fiscal years 2007, 2006 and 2005, the Company recognized revenues of $83,000, $103,000 and $238,000, respectively, from the sale of products to Beachside Produce and royalty revenues of $249,000, $264,000 and $233,000, respectively, from the use by Beachside Produce of Apio's trademarks. The related accounts receivable from Beachside Produce are classified as related party in the accompanying Consolidated Balance Sheets as of May 27, 2007 and May 28, 2006.

In addition, the Apio CEO has a 6% ownership interest in Apio Cooling LP, a limited partnership in which Apio is the general partner with a 60% ownership interest. Included in minority interest as of May 27, 2007 and May 28, 2006 is $227,000, and $237,000, respectively, related to the Apio CEO's ownership interest.

All related party transactions are monitored quarterly by the Company and approved by the Audit Committee of the Board of Directors.

Property and Equipment

Property and equipment are stated at cost. Expenditures for major improvements are capitalized while repairs and maintenance are charged to expense. Depreciation is expensed on a straight-line basis over the estimated useful lives of the respective assets, generally three to thirty years for buildings and leasehold improvements and three to seven years for furniture and fixtures, computers, capitalized software, machinery, equipment and autos. Leasehold improvements are amortized over the lesser of the economic life of the improvement or the life of the lease on a straight-line basis.

The Company capitalizes software development costs for internal use in accordance with Statement of Position 98-1, "*Accounting for Costs of Computer Software Developed or Obtained for Internal Use*" ("SOP 98-1"). Capitalization of software development costs begins in the application development stage and ends when the asset is placed into service. The Company amortizes such costs using the straight-line basis over estimated useful lives. The Company capitalized zero and $226,000 of software development costs during the years ended May 27, 2007 and May 28, 2006, respectively.

Intangible Assets

In June 2001, the Financial Accounting Standards Board issued Statements of Financial Accounting Standards No. 141, *Business Combinations*, and No. 142, *Goodwill and Other Intangible Assets* (SFAS 142), effective for fiscal years beginning after December 15, 2001. Under the new rules, goodwill and intangible assets deemed to have indefinite lives are no longer amortized but are subject to annual impairment tests in accordance with the Statements. Other intangible assets will continue to be amortized over their useful lives.

The Company is required under SFAS 142 to review goodwill and indefinite lived intangible assets at least annually. During fiscal year 2007, the Company completed its annual impairment review. The review is performed by grouping the net book value of all long-lived assets for reporting entities, including goodwill and other intangible assets, and comparing this value to the related estimated fair value. The determination of fair value is based on estimated future discounted cash flows related to these long-lived assets. The discount rate used was based on the risks associated with the reporting entities. The determination of fair value was performed by management using the services of an independent appraiser. The review concluded that the fair value of the reporting entities exceeded the carrying value of their net assets and thus no impairment charge was warranted as of May 27, 2007.

Equity Investment in Non-Public Company

The Company's equity investment in a non-public company is carried at cost, as adjusted for impairment losses, if any. Since there is no readily available market value information, the Company periodically reviews this investment to determine if any other than temporary declines in value have occurred and then the carrying value of the investment is adjusted as necessary.

1. Organization, Basis of Presentation, and Summary of Significant Accounting Policies (continued)

Deferred Revenue

Cash received in advance of services performed (principally revenues related to upfront license fees) are recorded as deferred revenue. At May 27, 2007, $10.3 million has been recognized as a liability for deferred license fee revenues associated with the Monsanto transactions (Note 2) and $160,000 for advances on ground lease payments from growers.

At May 28, 2006, $600,000 has been recognized as a liability for deferred license fee revenues and $211,000 for advances on ground lease payments from growers.

Minority Interest

In connection with the acquisition of Apio, Landec acquired Apio's 60% general partner interest in Apio Cooling, a California limited partnership. Apio Cooling is included in the consolidated financial statements of Landec for all periods presented. The minority interest balance of $1.8 million, at May 27, 2007 is comprised of $1.6 million of limited partners' interest in Apio Cooling LP and $261,000 of third party ownership in Apio. The minority interest balance of $1.8 million at May 28, 2006 is comprised of $1.5 million of limited partners' interest in Apio Cooling LP and $296,000 of third party ownership in Apio.

Income Taxes

The Company accounts for income taxes using the liability method. Under this method, deferred tax assets and liabilities are determined based on differences between financial reporting and tax bases of assets and liabilities and are measured using enacted tax rates and laws that will be in effect when the differences are expected to reverse. Valuation allowances are provided when it is more likely than not that all or a portion of a deferred tax asset will not be realized. In determining whether a valuation allowance is warranted, the Company takes into account such factors as prior earnings history, expected future earnings, carry-back and carry forward periods, and tax strategies that could potentially enhance the likelihood of realization of a deferred tax asset.

Per Share Information

Financial Accounting Standards Board issued Statement No. 128, "*Earnings Per Share*" (SFAS 128) requires the presentation of basic and diluted earnings per share. Basic earnings per share excludes any dilutive effects of options, warrants and convertible securities and is computed using the weighted average number of common share outstanding. Diluted earnings per share reflects the potential dilution if securities or other contracts to issue common stock were exercised or converted into common stock. Diluted common equivalent shares consist of stock options using the treasury stock method.

The following table sets forth the computation of diluted net income per share (in thousands, except per share amounts):

	Fiscal Year Ended May 27, 2007	Fiscal Year Ended May 28, 2006	Fiscal Year Ended May 29, 2005
Numerator:			
Net income	$ 29,189	$ 8,651	$ 5,402
Less: Minority interest in income of subsidiary	(778)	(556)	(294)
Net income for diluted net income per share	$ 28,411	$ 8,095	$ 5,108

Denominator:						
Weighted average shares for basic net income per share		25,260		24,553		23,705
Effect of dilutive securities:						
Stock options		1,298		1,104		909
Weighted average shares for diluted net income per share		26,558		25,657		24,614
Diluted net income per share	$	1.07	$	0.32	$	0.21

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1. Organization, Basis of Presentation, and Summary of Significant Accounting Policies (continued)

Options to purchase 81,030, 276,313 and 622,452 shares of Common Stock at a weighted average exercise price of $8.86, $6.70 and $6.78 per share were outstanding during fiscal years ended May 27, 2007, May 28, 2006 and May 29, 2005, respectively, but were not included in the computation of diluted net income per share because the options' exercise price were greater than the average market price of the Common Stock and, therefore, the effect would be antidilutive.

Cost of Sales

The Company includes in cost of sales all the costs related to the sale of products in accordance with generally accepted accounting principles. These costs include the following: raw materials (including produce, seeds and packaging), direct labor, overhead (including indirect labor, depreciation, and facility related costs) and shipping and shipping related costs.

Research and Development Expenses

Costs related to both research contracts and Company-funded research is included in research and development expenses. Costs to fulfill research contracts generally approximate the corresponding revenue. Research and development costs are primarily comprised of salaries and related benefits, supplies, travel expenses and corporate allocations.

Accounting for Stock-Based Compensation

On May 29, 2006, the Company adopted SFAS 123R, which is a revision of SFAS No. 123 "Accounting for Stock-Based Compensation" ("SFAS 123"), and supersedes APB No. 25, "Accounting for Stock Issued to Employees" ("APB 25"). Among other items, SFAS 123R requires companies to record compensation expense for stock-based awards issued to employees and directors in exchange for services provided. The amount of the compensation expense is based on the estimated fair value of the awards on their grant dates and is recognized over the required service periods. The Company's stock-based awards include stock option grants and restricted stock unit awards (RSUs).

Prior to the adoption of SFAS 123R, the Company applied the intrinsic value method set forth in APB 25 to calculate the compensation expense for stock-based awards. The Company has historically set the exercise price for its stock options equal to the market value on the grant date. As a result, the options had no intrinsic value on their grant dates, and therefore the Company did not record any compensation expense unless the terms of the stock options were subsequently modified. For RSUs, the calculation of compensation expense under APB 25 and SFAS 123R is similar except for the accounting treatment for forfeitures as discussed below.

The Company adopted SFAS 123R using the modified prospective transition method, which requires the application of the accounting standard to (i) all stock-based awards issued on or after May 29, 2006 and (ii) any outstanding stock-based awards that were issued but not vested as of May 29, 2006. Accordingly, the Company's consolidated financial statements as of May 28, 2006 and May 29, 2005, and for the fiscal years then-ended, were accounted for under the provisions of APB 25. During the fiscal year ended May 27, 2007, the Company recognized stock-based compensation expense of $615,000 which included $160,000 for restricted stock unit awards and $455,000 for stock option grants, respectively.

The following table summarizes the stock-based compensation by income statement line item:

	Fiscal Year Ended

		May 27, 2007
Research and development	$	82,000
Sales, general and administrative	$	533,000
Total stock-based compensation expense	$	615,000

1. Organization, Basis of Presentation, and Summary of Significant Accounting Policies (continued)

The estimated fair value for stock options, which determines the Company's calculation of compensation expense, is based on the Black-Scholes option pricing model. Upon the adoption of SFAS 123R, the Company changed its method of calculating and recognizing the fair value of stock-based compensation arrangements to the straight-line, single-option method. Compensation expense for all stock option and restricted stock awards granted prior to May 29, 2006 will continue to be recognized using the straight-line, multiple-option method. In addition, SFAS 123R requires the estimation of the expected forfeitures of stock-based awards at the time of grant. As a result, the Company uses historical data to estimate pre-vesting forfeitures and records stock-based compensation expense only for those awards that are expected to vest and revises those estimates in subsequent periods if the actual forfeitures differ from the prior estimates. In the pro-forma information required under SFAS 123R for periods prior to May 29, 2006, the Company accounted for forfeitures as they occurred.

Valuation Assumptions

As of May 27, 2007, May 28, 2006 and May 29, 2005, the fair value of stock option grants was estimated using the Black-Scholes option pricing model. The following weighted average assumptions were used:

	Landec Employee Stock Options		
	Fiscal Year Ended May 27, 2007	**Fiscal Year Ended May 28, 2006**	**Fiscal Year Ended May 29, 2005**
Expected life (in years)	4.27	4.58	4.38
Risk-free interest rate	5.08%	4.37%	3.70%
Volatility	0.51	0.52	0.57
Dividend yield	0%	0%	0%

The Black-Scholes option pricing model requires the input of highly subjective assumptions, including the expected stock price volatility. The change in the volatility in the fiscal years ended May 27, 2007, May 28, 2006 and May 29, 2005 is a result of basing the volatility on Landec's stock price.

The weighted average estimated fair value of Landec employee stock options granted at grant date market prices during the fiscal years ended May 27, 2007, May 28, 2006 and May 29, 2005 was $4.15, $3.36 and $3.54 per share, respectively. No stock options were granted above or below grant date market prices during the fiscal years ended May 27, 2007, May 28, 2006 and May 29, 2005. The weighted average estimated fair value of shares granted under the Landec Employee Stock Purchase Plan during the fiscal years ended May 27, 2007, May 28, 2006 and May 29, 2005 was $2.19, $2.19 and $1.98 per share, respectively.

1. Organization, Basis of Presentation, and Summary of Significant Accounting Policies (continued)

For purposes of pro forma disclosures, the estimated fair value of the options is amortized to expense over the service period of the options using the straight-line method. The Company's pro forma information follows (in thousands except for per share data):

		Year Ended May 28, 2006		Year Ended May 29, 2005
Net income - as reported	$	8,651	$	5,402
Deduct:				
Stock-based employee expense determined under SFAS 123		(1,160)		(1,511)
Pro forma net income	$	7,491	$	3,891
Basic net income per share - as reported	$	0.35	$	0.23
Diluted net income per share - as reported	$	0.32	$	0.21
Basic pro forma net income per share	$	0.31	$	0.16
Diluted pro forma net income per share	$	0.27	$	0.15

Recent Accounting Pronouncements

Fair Value Measurements

In September 2006, the FASB issued SFAS No. 157, "Fair Value Measurements" ("SFAS 157"). SFAS 157 defines fair value, establishes a framework for measuring fair value and expands disclosure of fair value measurements. SFAS 157 applies under other accounting pronouncements that require or permit fair value measurements and accordingly, does not require any new fair value measurements. SFAS 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007. The Company has not determined the impact of the adoption of SFAS 157 on its consolidated financial statements.

Accounting for Uncertainty in Income Taxes

In June 2006, the Financial Accounting Standards Board ("FASB") issued FASB Interpretation No. 48, *Accounting for Uncertainty in Income Taxes — an Interpretation of FASB Statement No. 109* ("FIN No. 48"), which clarifies the accounting for uncertainty in income taxes recognized in an enterprise's financial statements in accordance with FASB Statement No. 109, *Accounting for Income Taxes*. FIN No. 48 prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. FIN No. 48 also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure, and transition and defines the criteria that must be met for the benefits of a tax position to be recognized. The provisions of FIN No. 48 will be effective for the Company commencing at the start of fiscal 2008, May 28, 2007. The Company is currently evaluating the impact of adopting FIN No. 48 on its consolidated financial statements, however, the Company does not expect the adoption of FIN No. 48 to have a material impact on the Company's consolidated financial statements.

2. Sale of Fielder's Choice Direct and License Agreement

On December 1, 2006, Landec sold its direct marketing and sales seed company FCD, which included the Fielder's Choice Direct® and Heartland Hybrid® brands, to American Seeds, Inc. (ASI), a wholly owned subsidiary of Monsanto Company. The acquisition price for FCD was $50 million in cash paid at the close. In addition, the Company could have earned up to an additional $5 million based on FCD results for the twelve months ended May 31, 2007. None of the earn-out was earned. During the fiscal year 2007, Landec recorded income from the sale, net of direct expenses and bonuses, of $22.7 million. The income that was recorded is equal to the difference between the fair value of FCD of $40 million and its net book value, less direct selling expenses and bonuses. In accordance with generally accepted accounting principles, the portion of the $50 million of proceeds in excess of the fair value of FCD, or $10 million, will be allocated to the technology license agreement described below and will be recognized as revenue ratably over the five year term of the technology license agreement or $2 million per year beginning December 1, 2006. The fair value was determined by management with the assistance of an independent appraiser.

The following summarizes sales proceeds allocated to the technology license agreement and the net income from the sale of FCD (in thousands):

Cash received at close	$	50,000
Fair market value of FCD		40,000
Proceeds allocated to technology license agreement (1)	$	10,000
Fair market value of FCD	$	40,000
Less: Cost basis of assets sold net of liabilities assumed (2)		(14,856)
Less: Direct expenses of sale		(557)
Net gain from sale of FCD		24,587
Less: Bonuses paid to employees as a result of the sale		(1,918)
Income from sale of FCD	$	22,669

(1) Represents a deferred gain at the closing date which will be recognized as revenue over 5 years as described below.

(2) Included in assets held for sale in the accompanying Consolidated Balance Sheets at May 28, 2006 is $5.4 million in cash which was retained by the Company upon the close of the sale of FCD.

As a result of the sale of FCD, the Company recorded an income tax expense of $2.5 million in fiscal year 2007 for state income taxes and federal AMT.

On December 1, 2006, Landec also entered into a five-year co-exclusive technology license and polymer supply agreement ("the Agreement") with Monsanto Company for the use of Landec's Intellicoat polymer seed coating technology. Under the terms of the Agreement, Monsanto will pay Landec $2.6 million per year in exchange for (1) a co-exclusive right to use Landec's Intellicoat temperature-activated seed coating technology worldwide during the license period, (2) the right to be the exclusive global sales and marketing agent for the Intellicoat seed coating technology, and (3) the right to purchase the technology at any time during the five year term of the Agreement. Monsanto will also fund all operating costs, including all Intellicoat research and development, product development and non-replacement capital costs during the five year agreement period. For the fiscal year ended May 27, 2007, Landec recognized $2.7 million in revenues and income from the Agreement.

The Agreement also provides for a fee payable to Landec of $4 million if Monsanto elects to terminate the agreement or $8 million if Monsanto elects to buyout the technology. If the purchase option is exercised before the fifth anniversary of the Agreement, or if Monsanto elects to terminate the Agreement, all annual license fees and supply

payments that have not been paid to Landec will become due upon the purchase. If Monsanto does not exercise its purchase option by the fifth anniversary of the Intellicoat agreement, Landec will receive the termination fee and all rights to the Intellicoat seed coating technology will revert to Landec. Accordingly, Landec will receive minimum guaranteed payments of $17 million for license fees and polymer supply payments over five years or $21 million in maximum payments if Monsanto elects to buyout the licensed technology. The minimum guaranteed payments and the deferred gain of $2 million per year described above will result in Landec recognizing revenue and operating income of $5.4 million per year for fiscal years 2008 through 2011 and $2.7 million per year for fiscal years 2007 and 2012.

2. Sale of Fielder's Choice Direct and License Agreement (continued)

If Monsanto elects to purchase the technology, an additional $4 million of license fee revenue will be recognized at the time of purchase. If Monsanto exercises its purchase option, Landec and Monsanto will enter into a new long-term supply agreement in which Landec will continue to be the exclusive supplier of Intellicoat polymer materials to Monsanto.

In conjunction with the sale of FCD, Landec purchased all of the outstanding common stock and options of Landec Ag not owned by Landec at the fair market value of each share as if all options had been exercised as of December 1, 2006. The fair market value was $7.4 million which was funded with proceeds from the sale of FCD. After the purchase, Landec Ag became a wholly owned subsidiary of Landec. In accordance with SFAS 123R, this purchase did not result in additional compensation expense to the Company as all of the stock and options purchased were fully vested at the time of the purchase and the consideration paid was equal to the fair value on the date of the purchase. The purchase of Landec Ag's outstanding common stock and options was recorded to retained earnings.

Excluding the $2.7 million in revenues from the Agreement, Landec Ag revenues for the fiscal years 2007 and 2006 were $131,000 and $34.1 million, respectively. The net operating losses for Landec Ag, excluding the income from the sale of FCD and the $2.7 million in license fees from the Agreement, for fiscal year 2007 were $5.8 million compared to net operating income of $353,000 in fiscal year 2006. Landec Ag had cash balances at May 28, 2006 of $5.4 million.

3. Purchase of Heartland Hybrids Assets

On August 29, 2005, Landec Corporation, through its agricultural seed subsidiary, Landec Ag, Inc., acquired the assets of Heartland Hybrids, Inc. ("Heartland"), which is based in Dassel, MN, for $6.0 million. The consideration at closing consisted of 152,186 shares of Landec Common Stock valued at $960,000 and cash of $3.69 million. In addition, the Company incurred $130,000 in acquisition related expenses. The agreement also provides for future payments to the former owners of Heartland of up to $1.35 million. These payments consist of a cash earn-out of $1.2 million based on Heartland achieving certain financial targets for fiscal years 2006 and 2007 and a $150,000 hold back for any post closing adjustments, $100,000 of which was earned and paid in fiscal year 2006, the remaining $50,000 was paid in fiscal year 2007. Heartland operations are included in Landec's consolidated results of operations commencing August 29, 2005. The purchase price has been allocated to the acquired assets and liabilities based on their relative fair market values, subject to final adjustments predominantly related to earn-out payments. These allocations are based on independent valuations and other studies.

On August 28, 2006 the Company amended the Heartland Asset Purchase Agreement. In accordance with the amendment the Company paid the former owners of Heartland a cash earn out payment of $1.0 million. In exchange for the Company accelerating the earn out payment, the former owners of Heartland agreed to reduce the total potential earn out by $200,000 from the original earn out potential of $1.2 million. The Company recorded $383,000 of the earn out to goodwill during the first quarter of fiscal year 2007, the remaining $617,000 was recorded to goodwill during the Company's second quarter of fiscal year 2007.

The following is a summary of the purchase price allocation (in thousands):

Net assets and liabilities	$	(757)
Customer Base		800
Trademark		1,700
Goodwill		4,187
	$	5,930

On December 1, 2006, Landec sold its direct marketing and sales seed company FCD, which included the Fielder's Choice Direct and Heartland Hybrid brands, to ASI (see Note 2).

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4. License Agreements

On December 23, 2005, Landec entered into an exclusive licensing agreement with Aesthetic Sciences Corporation ("Aesthetic Sciences"), a medical device company. Aesthetic Sciences paid Landec an upfront license fee of $250,000 for the exclusive rights to use Landec's IntelimerÒ materials technology for the development of dermal fillers worldwide. Landec will also receive royalties on the sale of products incorporating Landec's technology. In addition, the Company received shares of preferred stock valued at $1.31 million which represents a 19.9% ownership interest in Aesthetic Sciences. The $1.31 million is included in other assets in the accompanying Consolidated Balance Sheet. The $1.56 million of value received under this agreement is recorded as licensing revenue in fiscal year 2006 in the accompanying Consolidated Statements of Operations since Landec has no further obligations under this agreement.

As part of the original agreement with Aesthetic Sciences, Landec was to receive additional shares upon the completion of a specific milestone. On November 22, 2006, that milestone was met and as a result Landec received an additional 800,000 shares of preferred stock valued at $481,000. The receipt of the additional 800,000 preferred shares did not change Landec's 19.9% ownership interest in Aesthetic Sciences. The $481,000 is included in other assets in the accompanying Consolidated Balance Sheet and is recorded as licensing revenue for fiscal year 2007 in the accompanying Consolidated Statements of Operations since Landec has no further obligations under this agreement.

On March 14, 2006, Landec entered into an exclusive license and research and development agreement with Air Products and Chemicals, Inc. Landec received an upfront licensing fee of $800,000 at close and will receive up to an additional $1.6 million of license payments that will be paid in quarterly installments of $200,000 each during years two and three of the agreement for the exclusive rights to use Landec's Intelimer materials technology in specific fields worldwide. The first installment for $200,000 was received during the fourth quarter of fiscal year 2007. In addition, Landec received at close $100,000 for technology transfer work that was performed by Landec prior to May 28, 2006. Landec will provide research and development support to Air Products for three years with a mutual option for two additional years. The license fees will be recognized as license revenue over a three year period beginning March 2006. In addition, in accordance with the agreement, Landec will receive 40% of the gross profit generated from the sale of products by Air Products occurring after April 1, 2007, that incorporate Landec's Intelimer materials. The Company recognized $300,000 in license revenues under this agreement during the fourth quarter of fiscal year 2006 and $800,000 during fiscal year 2007. The Company also recognized $20,000 during the fourth quarter of fiscal year 2007 for its share of gross profit realized from April 1, 2007 through May 27, 2007.

5. Purchase and Sale of Fruit Land

On January 14, 2005, the Company entered into an agreement to purchase approximately 155 acres of fruit land from an individual for $812,500. This amount was paid to the seller through the funding of an escrow account on March 23, 2005. In a separate unrelated transaction, on January 31, 2005, the Company entered into an agreement to sell approximately 45 acres of grape land to an individual for $452,500. Upon entering into the agreement, the Company received $28,000 in cash and promissory notes receivable for $424,500. The sale closed on January 3, 2006. During fiscal year 2006, $56,000 of payments were made on the notes receivable. The remaining balance of $368,500 was paid in full during fiscal year 2007. In another transaction which closed on January 17, 2006, the Company sold to an individual the remaining 110 acres for $936,000 in cash, net of sales commissions. The Company recorded a gain of $160,000 during fiscal year 2006 on these sales.

6. Insurance Settlement

On August 25, 2006 the Company received a cash payment of $1.6 million from the settlement of insurance claims associated with a fire that occurred at its Dock Resins facility in February 2000. The settlement resulted in the Company recording a reduction to selling, general and administrative expenses of $1.3 million, net of expenses, during the Company's first quarter of fiscal year 2007. In addition, $381,000 had been placed in escrow pending the

outcome of certain disputed professional fees. In September 2006, the Company resolved the fee dispute and paid professional fees of $227,000 from the escrow and received the balance of $154,000 which the Company recorded as a reduction to selling, general and administrative expenses during fiscal year 2007 .

7. Notes and Advances Receivable

	May 27, 2007	May 28, 2006
Notes and advances receivable at May 27, 2007 and May 28, 2006 consisted of the following (in thousands):		
Note receivable due from buyer of fruit processing equipment in annual installments of $98 plus interest at prime rate plus 1.0%, with final payment due October 20, 2009, secured by purchased assets (2)	$ 205	$ 413
Note receivable due from grower in annual installments in an amount equal to 50% of net profits realized by borrower from the sale of grapes produced from this property, plus interest at prime (8.00% at May 28, 2006), with final payment due December 31, 2009, secured by a deed of trust (2)	—	380
Advances to a grower under an agricultural sublease in semi-annual installments of $215 through October 31, 2006, to be repaid at $12 per week by withholding proceeds from crop produced on this property (1)	—	156
Note receivable due from grower in annual installments of $33 plus interest at prime rate plus 1.0%, with final payment due December 31, 2007, unsecured (1)	33	67
Note receivable due from Beachside Produce (related party) in monthly installments of $7 including interest at 5%, with final payment due June 30, 2006, secured by lien and security interest (2)	—	14
Advances to a grower under agricultural subleases in semi-annual installments of $144 and a single installment of $54, to be repaid at $12 per week by withholding proceeds from crop produced on this property. Leases expire October 31, 2009 and August 1, 2007 (1)	140	—
Notes receivable due from growers, with principal and interest of prime rate plus 1.75%, secured by their respective partnership interest in Apio Cooling LP. Payments to be deducted from distributions until notes are paid in full, with balances due December 31, 2008 (1)	—	4
Note receivable due from buyer of fruit trademarks in annual installments of $3 plus interest at prime rate plus 1.0%, with final payment due October 20, 2009 (2)	—	12
Gross notes and advances receivable	378	1,046
Less allowance for doubtful notes	—	(25)
Net notes and advances receivable	378	1,021
Less current portion of notes and advances receivable	(282)	(390)
Non-current portion of notes and advances receivable	$ 96	$ 631

(1) Represents notes and advances receivable associated with operating activities.

(2) Represents notes and advances receivable associated with investing activities.

Interest income from interest bearing notes receivable for the fiscal years ended May 27, 2007, May 28, 2006 and May 29, 2005 was $52,000, $89,000 and $62,000, respectively.

8. Property and Equipment

Property and equipment consists of the following (in thousands):

	Years of Useful Life	May 27, 2007	May 28, 2006
Land and building	15-30	$ 16,783	$ 10,323
Leasehold improvements	3-20	1,031	1,102
Computer, capitalized software, machinery, equipment and auto	3-7	20,383	19,737
Furniture and fixtures	5-7	456	448
Construction in process		204	2,042
Gross property and equipment		38,857	33,652
Less accumulated depreciation and amortization		(18,587)	(16,770)
Net property and equipment		$ 20,270	$ 16,882

Depreciation expense for the fiscal years ended May 27, 2007, May 28, 2006 and May 29, 2005 was $3.3 million, $3.2 million and $3.4 million, respectively. Equipment under capital leases, which is the security for the related lease obligation, at May 27, 2007 and May 28, 2006 was $104,000 and $103,000, respectively. The related accumulated amortization for equipment under capital leases at May 27, 2007 and May 28, 2006 was $78,000 and $58,000, respectively. Amortization related to capitalized software was $666,000, $661,000 and $742,000, respectively, for fiscal years ended May 27, 2007, May 28, 2006 and May 29, 2005. The unamortized computer software costs at May 27, 2007 and May 28, 2006 were $594,000 and $2.1 million, respectively.

9. Intangible Assets

Changes in the carrying amount of goodwill for the fiscal years ended May 27, 2007, May 28, 2006 and May 29, 2005 by reportable segment, are as follows (in thousands):

	Food Products Technology	Agricultural Seed Technology	Total
Balance as of May 30, 2004	$ 21,233	$ 4,754	$ 25,987
Goodwill changes during the period	—	—	—
Balance as of May 29, 2005	21,233	4,754	25,987
Goodwill acquired during the period	—	3,137	3,137
Reclassed to assets held for sale		(7,876)	(7,876)
Balance as of May 28, 2006	21,233	15	21,248
Goodwill acquired during the period	169	1,050	1,219
Goodwill sold and amortized during the period	—	(1,065)	(1,065)
Balance as of May 27, 2007	$ 21,402	$ —	$ 21,402

Information regarding Landec’s other intangible assets is as follows (in thousands):

	Trademarks	Other	Total
Balance as of May 30, 2004	$ 11,570	85	$ 11,655
Amortization expense	—	(27)	(27)
Balance as of May 29, 2005	11,570	58	11,628
Other intangibles acquired	1,700	810	2,510

Reclassed to assets held for sale	(5,042)	(860)	(5,902)
Amortization expense	—	(8)	(8)
Balance as of May 28, 2006	8,228	—	8,228
Amortization expense	—	—	—
Balance as of May 27, 2007	$ 8,228	$ —	$ 8,228

Amortization expense, including amortization of other assets, for fiscal years 2007, 2006 and 2005 was $0, $0 and $103,000 for Food Products Technology and $0, $8,000 and $1,000 for Agricultural Seed Technology, respectively. Amortization expense, including amortization of other assets, for fiscal years ended May 27, 2007, May 28, 2006 and May 29, 2005 was $0, $8,000 and $104,000, respectively.

10. Shareholders' Equity

Holders of Common Stock are entitled to one vote per share.

Convertible Preferred Stock

The Company has authorized two million shares of preferred stock, and as of May 27, 2007 has no outstanding preferred stock.

Common Stock, Stock Purchase Plans and Stock Option Plans

At May 27, 2007, the Company had 2,806,403 common shares reserved for future issuance under Landec stock option plans.

On October 14, 2005, following shareholder approval at the Annual Meeting of Shareholders of the Company, the 2005 Stock Incentive Plan (the "Plan") became effective. The Plan replaced the Company's four then existing equity plans and no shares remain available for grant under these existing plans. Employees (including officers), consultants and directors of the Company and its subsidiaries and affiliates are eligible to participate in the Plan.

The Plan provides for the grant of stock options (both nonstatutory and incentive stock options), stock grants, stock units and stock appreciation rights. Awards under the Plan will be evidenced by an agreement with the Plan participant. Under the Plan, 861,038 shares of the Company's Common Stock ("Shares") were initially available for awards, and as of May 27, 2007, 705,898 shares were available for awards. Under the Plan no recipient may be awarded any of the following during any fiscal year: (i) stock options covering in excess of 500,000 Shares; (ii) stock grants and stock units covering in excess of 250,000 Shares in the aggregate; or (iii) stock appreciation rights covering more than 500,000 Shares. In addition, awards to non-employee directors are discretionary. However, a non-employee director may not be granted awards covering in excess of 30,000 Shares in the aggregate during any fiscal year.

The 1995 Directors' Stock Option Plan (the "Directors' Plan") provided that each person who became a non- employee director of the Company, who has not received a previous grant, shall be granted a nonstatutory stock option to purchase 20,000 shares of Common Stock on the date on which the optionee first becomes a non-employee director of the Company. Thereafter, on the date of each annual meeting of the shareholders each non-employee director shall be granted an additional option to purchase 10,000 shares of Common Stock if, on such date, he or she shall have served on the Company's Board of Directors for at least six months prior to the date of such annual meeting. The exercise price of the options is the fair market value of the Company's Common Stock on the date the options are granted. Options granted under this plan are exercisable and vest upon grant.

The 1996 Non-Executive Stock Option Plan authorized the Board of Directors to grant non-qualified stock options to employees, including executive officers, and outside consultants of the Company. The exercise price of the options was equal to the fair market value of the Company's Common Stock on the date the options were granted. Options are generally exercisable upon vesting and generally vest ratably over four years and are subject to repurchase if exercised before being vested.

The 1996 Stock Option Plan authorized the Board of Directors to grant stock purchase rights, incentive stock options or non-statutory stock options to Landec executives. The exercise price of the stock purchase rights, incentive stock options and non-statutory stock options may be no less than 100% of the fair market value of Landec's Common Stock on the date the options were granted. Options generally are exercisable upon vesting, generally vest ratably over four years and are subject to repurchase if exercised before being vested.

The New Executive Stock Option Plan authorized the Board of Directors to grant non-statutory stock options to officers of Landec or officers of Apio or Landec Ag whose employment with each of those companies began after October 24, 2000. The exercise price of the non-statutory stock options may be no less than 100% and 85%, for named executives and non-named executives, respectively, of the fair market value of Landec's Common Stock on the date the options were granted. Options generally are exercisable upon vesting, generally vest ratably over four years and are subject to repurchase if exercised before being vested.

10. Shareholders' Equity (continued)

On April 15, 2005, the Board of Directors of the Company approved the accelerated vesting of all unvested options previously granted to employees under the Company's 1996 Stock Option Plans (collectively, the "Plans") which have an exercise price greater than $6.25 (the "Acceleration") the closing price of the Company's Common Stock on April 15, 2005 in order to avoid recognizing an expense in future periods upon the adoption of SFAS 123R.

Pursuant to the Acceleration, options granted under the Plans to purchase 192,026 shares of the Company's common stock that would otherwise have vested at various times within three years from April 15, 2005 became fully vested. As a result of the Board's decision to approve the Acceleration, each option agreement underlying options subject to the Acceleration is deemed to be amended to reflect the Acceleration as of the effective date, but all other terms and conditions of each such option agreement remains in full force and effect. On the date of the Acceleration no compensation expense was recorded because the fair market value of the Company's Common Stock was below the exercise price of the options that were accelerated.

Employee Stock Purchase Plan. The Company had an employee stock purchase plan which permitted eligible employees to purchase Common Stock, which may not exceed 10% of an employee's compensation, at a price equal to the lower of 85% of the fair market value of the Company's Common Stock at the beginning of the offering period or on the purchase date. The Company issued 869,271 shares under the Employee Stock Purchase Plan prior to it being terminated on June 1, 2006.

Activity under all Landec Stock Option Plans is as follows:

Stock-Based Compensation Activity

	Restricted Stock Outstanding			Stock Options Outstanding	
	RSUs and Options Available for Grant	Number of Restricted Shares	Weighted Average Grant Date Fair Value	Number of Stock Options	Weighted Average Exercise Price (Fair Value)
Balance at May 30, 2004	1,538,545	—	—	3,922,761	$ 4.81
Granted	(625,000)	—	—	625,000	$ 6.54
Exercised	—	—	—	(397,772)	$ 3.80
Forfeited	27,493	—	—	(27,493)	$ 4.98
Balance at May 29, 2005	941,038	—	—	4,122,496	$ 5.08
Additional shares reserved	861,038	—	—	—	—
Granted	(83,333)	833	$ 7.53	82,500	$ 6.68
Exercised	—	—	—	(1,027,718)	$ 5.83
Forfeited	59,762	—	$ 7.53	(59,762)	$ 6.36
Terminated plans	(920,800)	—	—	—	—
Balance at May 28, 2006	857,705	833	$ 7.53	3,117,516	$ 4.85
Granted	(153,335)	38,335	$ 8.86	115,000	$ 8.86
Exercised	—	—	—	(1,163,234)	$ 4.72
Forfeited	8,778	(833)	$ 7.53	(7,945)	$ 4.93
Plan shares expired	(6,417)	—	—	—	—
Balance at May 27, 2007	706,731	38,335	$ 8.86	2,061,337	$ 5.14

Included in exercises for fiscal year 2007 are 207,112 options that were exercised through a net share settlement transaction (no cash) to pay for the exercise price of the options and the related taxes due on the exercise.

10. Shareholders' Equity (continued)

The following table summarizes information concerning stock options outstanding and exercisable at May 27, 2007:

	Options Outstanding				Options Exercisable		
Range of Exercise Prices	Number of Shares Outstanding (in years)	Weighted Average Remaining Contractual Life (in years)	Weighted Average Exercise Price	Aggregate Intrinsic Value	Number of Shares Exercisable	Weighted Average Exercise Price	Aggregate Intrinsic Value
1.660 - $$3.250	289,393	5.08	$ 2.91	$ 3,082,035	288,767	$ 2.91	$ 3,075,369
3.375 - $$3.375	278,000	3.53	$ 3.38	$ 2,830,040	278,000	$ 3.38	$ 2,830,040
3.400 - $$3.700	206,146	3.20	$ 3.47	$ 2,080,013	205,832	$ 3.47	$ 2,076,845
3.750 - $$4.938	217,323	3.54	$ 4.48	$ 1,973,293	217,323	$ 4.48	$ 1,973,293
5.000 - $$6.125	165,503	1.95	$ 5.51	$ 1,332,299	159,565	$ 5.50	$ 1,286,094
6.130 - $$6.130	262,000	4.98	$ 6.13	$ 1,946,660	187,000	$ 6.13	$ 1,389,410
6.450 - $$6.750	340,000	4.49	$ 6.68	$ 2,339,200	340,000	$ 6.68	$ 2,339,200
6.790 - $$8.860	302,972	6.92	$ 7.75	$ 1,760,267	243,937	$ 7.49	$ 1,480,698
1.660 - $$8.860	2,061,337	4.43	$ 5.14	$ 17,343,807	1,920,424	$ 4.99	$ 16,450,949

At May 27, 2007 and May 28, 2006 options to purchase 1,920,424 and 2,934,930 shares of Landec’s Common Stock were vested, respectively. No options have been exercised prior to being vested.

The aggregate intrinsic value in the table above represents the total pretax intrinsic value, based on the Company’s closing stock price of $13.56 on May 25, 2007, which would have been received by holders of stock options had all holders of stock options exercised their stock options that were in-the-money as of that date. The total number of in-the-money stock options exercisable as of May 27, 2007, was approximately 1.9 million shares. The aggregate intrinsic value of stock options exercised during the fiscal year 2007 was $8.8 million.

Shares Subject to Vesting

The following table summarizes the activity relating to unvested stock option grants and RSUs during the fiscal year ended May 27, 2007:

	Stock Options		Restricted Stock	
	Shares	Weighted Average Fair Value	Shares	Weighted Average Fair Value

Unvested at May 28, 2006	182,586	$	2.43	833	$	7.53
Granted	115,000	$	4.05	38,335	$	8.32
Vested/Awarded	(148,728)	$	2.44	—		—
Forfeited	(7,945)	$	3.27	(833)	$	7.53
Unvested at May 27, 2007	140,913	$	3.70	38,335	$	8.32

As of May 27, 2007, there was $691,000 of total unrecognized compensation expense related to unvested equity compensation awards granted under the Company's incentive stock plans. Total expense is expected to be recognized over the weighted-average period of 1.28 years.

As of May 27, 2007 the Company had reserved 2.8 million shares of common stock for future issuance under its current and former stock plans.

10. Shareholders' Equity (continued)

Landec Ag Stock Plan. Under the 1996 Landec Ag Stock Plan, the Board of Directors of Landec Ag could have granted stock purchase rights, incentive stock options or non-statutory stock options to employees and outside consultants. The exercise price of the stock purchase rights, incentive stock options and non-statutory stock options may be no less than 85%, 100% and 85%, respectively, of the fair market value of Landec Ag’s common stock as determined by Landec Ag’s Board of Directors. 2,000,000 shares were authorized to be issued under this plan. Options generally were exercisable upon vesting and generally vested ratably over four years and were subject to repurchase if exercised before being vested. The Landec Ag Stock Plan terminated on January 1, 2006.

The following table summarizes activity under the Landec Ag Stock Option.

		Outstanding Options	
	Options Available	Number of Shares	Weighted Average Exercise Price
Balance at May 30, 2004	414,068	1,259,850	$ 0.41
Options granted	—	—	—
Options exercised	—	(503,895)	$ 0.10
Options forfeited	165,855	(165,855)	$ 1.00
Balance at May 29, 2005	579,923	590,100	$ 0.71
Options granted	—	—	—
Options exercised	—	—	—
Options forfeited	52,313	(52,313)	$ 0.94
Expired in Plan	(632,236)	—	—
Balance at May 28, 2006	—	537,787	$ 0.69
Options granted	—	—	—
Options exercised	—	(59,462)	$ 0.24
Options forfeited	—	(625)	$ 1.00
Repurchased by Landec	—	(477,700)	$ 5.62
Balance at May 27, 2007	—	—	—

Apio Stock Plan. In connection with the acquisition of Apio, the Board of Directors of Landec authorized the establishment of the 1999 Apio Stock Option Plan ("1999 Plan"). Under the 1999 Plan, the Board of Directors of Apio may grant incentive stock options or non-statutory stock options to employees and outside consultants. The exercise price of the incentive stock options and non-statutory stock options may be no less than 100% and 85%, respectively, of the fair market value of Apio's common stock as determined by Apio's Board of Directors. Five million shares were authorized to be issued under this plan. Options were exercisable upon vesting and generally vested ratably over four years and were subject to repurchase if exercised before being vested. As of May 27, 2007, options for 2.0 million shares are outstanding under the 1999 Plan at an exercise price of $2.10 per share.

In May 2000, the 1999 Plan was terminated. All existing grants remain outstanding, and no future grants will be made from the plan. Concurrently, the 2000 Apio Stock Option Plan ("2000 Plan") was authorized by Apio's Board of Directors, which authorized the issuance of two million shares under the same terms and conditions as the 1999 Plan. As of May 27, 2007, options for 215,500 shares are outstanding under the 2000 Plan at an exercise price of $2.10 per share.

10. Shareholders' Equity (continued)

The following table summarizes activity under the Apio Stock Option Plan.

		Outstanding Options	
	Options Available	Number of Shares	Weighted Average Exercise Price
Balance at May 30, 2004	1,563,472	2,386,779	$ 2.10
Options granted	—	—	—
Options exercised	—	—	—
Options forfeited	59,457	(59,457)	$ 2.10
Balance at May 29, 2005	1,622,929	2,327,322	$ 2.10
Options granted	—	—	—
Options exercised	—	(50,158)	$ 2.10
Options forfeited	8,469	(8,469)	$ 2.10
Balance at May 28, 2006	1,631,398	2,268,695	$ 2.10
Options granted	—	—	—
Options exercised	—	(24,500)	$ 2.10
Options forfeited	28,695	(28,695)	$ 2.10
Balance at May 27, 2007	1,660,093	2,215,500	$ 2.10

At May 27, 2007, options to purchase 2,215,500 shares of Apio common stock were vested. As of May 27, 2007, the Company had 3,875,593 common shares reserved for future issuance under the Apio stock option plans.

11. Debt

Revolving Debt

On November 1, 2005, Apio amended its revolving line of credit with Wells Fargo Bank N.A. extending the term of the line to August 31, 2007. In addition, the line was reduced from $10.0 million to $7.0 million and outstanding amounts under the line of credit now bear interest at either the prime rate less 0.25% or the LIBOR adjustable rate plus 1.75% (7.07% at May 27, 2007). The revolving line of credit with Wells Fargo contains certain restrictive covenants, which require Apio to meet certain financial tests, including minimum levels of net income, maximum leverage ratio, minimum net worth and maximum capital expenditures. Landec has pledged substantially all of the assets of Apio to secure the line of credit with Wells Fargo. At May 27, 2007, no amounts were outstanding under the revolving line of credit. Apio has been in compliance or obtained waivers for loan covenants since the inception of this loan.

On August 29, 2006, Landec Ag amended and restated its revolving line of credit with Old National Bank which increased the line from $7.5 million to $10 million. In conjunction with the sale of FCD to ASI on December 1, 2006 (see Note 2 of Notes to Consolidated Financial Statements), Landec Ag’s line of credit was paid in full by ASI and subsequently terminated.

11. Debt (continued)

Long-Term Debt

Long-term debt consists of the following (in thousands):

	May 27, 2007	May 28, 2006
Note payable of Apio to a commercial finance company; due in monthly installments of $13 including variable interest currently at 7.23% with final payment due December 2019	$ —	$ 1,338
Note payable of Apio to a bank; due in monthly installments of $8 including variable interest currently at 7.76% with final payment due December 2015	—	630
Capitalized lease obligations in monthly installments of $2 with an interest rate of 5.90% with final payment due August 2008	28	50
	28	2,018
Less current portion	28	(2,018)
	$ —	$ —

The revolving note agreement contains various financial covenants including minimum fixed coverage ratio, minimum current ratio, minimum adjusted net worth and maximum leverage ratios.

Landec has pledged substantially all of Apio's assets to secure their revolving debt.

12. Income Taxes

The Company recorded an income tax provision based on the federal alternative minimum tax rate of $623,000 and state taxes of $1.833 million for a total tax amount of $2.5 million for the fiscal year ended May 27, 2007, $11,000 for the fiscal year ended May 28, 2006 and $6,000 for the fiscal year ended May 29, 2005. For fiscal years 2006 and 2005 the income tax expense is included in other expense in the accompanying Consolidated Statements of Income as the amounts are not material.

The actual provision for income taxes differs from the statutory U.S. federal income tax rate as follows (in thousands):

	Year Ended May 27, 2007	**Year Ended May 28, 2006**	**Year Ended May 29, 2005**
Provision at U.S. statutory rate (1)	$ 11,076	$ 2,949	$ 1,839
State income taxes, net of federal benefit	1,818	506	315
Change in valuation allowance	(10,026)	(3,788)	(2,017)
Tax credit carryforwards	(78)	375	(200)
Other	(334)	(31)	69
Total	$ 2,456	$ 11	$ 6

(1) Statutory rate was 35% for fiscal year 2007 and 34% for fiscal years 2006 and 2005.

As of May 27, 2007, the Company had federal and state net operating loss carryforwards of approximately $6.8 million and $100,000, respectively. These losses expire in different periods through 2025, if not utilized. The Company also had federal and state tax credit carryforwards of approximately $1.2 million and $800,000, respectively. The research and development tax credit carryforwards expire in different periods through 2026 for federal purposes and have an unlimited carryforward period for state purposes. The other state tax credit

carryforwards expire in different periods through fiscal year 2013.

12. Income Taxes (continued)

Utilization of the net operating losses and credits may be subject to a substantial annual limitation due to the ownership change limitations provided by the Internal Revenue Code of 1986. The annual limitation may result in the expiration of net operating losses and credits before utilization.

Significant components of the Company's deferred tax assets are as follows (in thousands):

	May 27, 2007	May 28, 2006
Deferred tax assets:		
Net operating loss carryforwards	$ 2,385	$ 14,900
Research and AMT credit carryforwards	2,495	2,100
Capitalized research and development	40	100
Other - net	(2,546)	(4,700)
Net deferred tax assets	2,374	12,400
Valuation allowance	(2,374)	(12,400)
Net deferred tax assets	$ —	$ —

Included in the other net deferred tax assets at May 27, 2007 is approximately $4.2 million of deferred tax liabilities that primarily relate to book/tax basis differences in fixed assets and intangibles.

Due to the Company's limited tax basis earnings history, the net deferred tax asset has been fully offset by a valuation allowance. The change in the valuation allowance was a decrease of $10 million and $3.5 million for the fiscal years ended May 27, 2007 and May 28, 2006, respectively, and an increase of $700,000 the fiscal year ended May 29, 2005. Approximately $800,000 of the valuation allowance for deferred tax assets as of May 27, 2007 relates to benefits of stock option deductions which, when recognized, will be allocated directly to contributed capital.

13. Commitments and Contingencies

Operating Leases

Landec leases facilities and equipment under operating lease agreements with various terms and conditions, which expire at various dates through 2010. The approximate future minimum lease payments under these operating leases, excluding land leases, at May 27, 2007 are as follows (in thousands):

	Amount
FY2008	$ 535
FY2009	352
FY2010	180
FY2011	29
FY2012	—
	$ 1,096

Rent expense for operating leases, including month to month arrangements was $1.4 million for the fiscal year ended May 27, 2007, $1.4 million for the fiscal year ended May 28, 2006 and $1.6 million for the fiscal year ended May 29, 2005

13. Commitments and Contingencies (continued)

Land Leases

Landec, through its Apio subsidiary, also leases farmland under various non-cancelable leases expiring through October 2009. Landec subleases substantially all of the farmland to growers on an annual basis. The subleases are generally non-cancelable and expire through October 2009. The approximate future minimum leases and sublease amounts receivable under farmland leases at May 27, 2007 are $766,000 through fiscal year 2010.

Rent income for land leases net of sublease rents, including month to month arrangements was $0 for the fiscal year ended May 27, 2007 and $25,000 for the fiscal year ended May 28, 2006. Rent expense for land leases net of sublease rents, including month to month arrangements was $51,000 for the fiscal year ended May 29, 2005.

Employment Agreements

Landec has entered into employment agreements with certain key employees. These agreements provide for these employees to receive incentive bonuses based on the financial performance of certain divisions in addition to their annual base salaries. The accrued incentive bonuses amounted to $631,000 at May 27, 2007 and $506,000 at May 28, 2006.

Licensing Agreement

In fiscal year 2001, the Company entered into an agreement for the exclusive worldwide rights to market grapes under certain brand names. Under the terms of the amended agreement (amended in fiscal year 2004), the Company is obligated to make annual payments of $100,000 for fiscal years 2008 through 2012.

Purchase Commitments

At May 27, 2007, the Company was committed to purchase $1.9 million of produce during fiscal year 2008 in accordance with contractual terms. Payments of $2.1 million were made in fiscal year 2007 under these arrangements.

14. Employee Savings and Investment Plans

The Company sponsors a 401(k) plan which is available to substantially all of the Company's employees.

Landec's Corporate Plan, which is available to all Landec employees ("Landec Plan"), allows participants to contribute from 1% to 50% of their salaries, up to the Internal Revenue Service (IRS) limitation into designated investment funds. Beginning in fiscal year 2001, the Company amended the plan so that it contributes an amount equal to 50% of the participants' contribution up to 3% of the participants' salary. In May 2003, the Company again amended the plan to make the Company's matching contribution to the plan on behalf of participants voluntary, and to make employees participation in the plan voluntary. In June 2006, the Company again amended the plan to increase the company match from 50% on the first 6% contributed by an employee to 67% on the first 6% contributed. Participants are at all times fully vested in their contributions. The Company's contribution vests over a four-year period at a rate of 25% per year. The Company retains the right, by action of the Board of Directors, to amend, modify, or terminate the plan. For the fiscal years ended May 27, 2007, May 28, 2006 and May 29, 2005, the Company contributed $401,000, $335,000 and $294,000, respectively, to the Landec Plan.

15. Business Segment Reporting

Landec operates in two business segments: the Food Products Technology segment and the Agricultural Seed Technology segment. The Food Products Technology segment markets and packs produce and specialty packaged fresh-cut vegetables that incorporate the Intelimer packaging technology for the fresh-cut and whole produce industry through its Apio subsidiary. Prior to the sale of FCD to ASI on December 1, 2006 (Note 2), the Agricultural Seed Technology segment marketed and distributed hybrid seed corn to the farming industry and as a result of the license agreement with Monsanto is still selling seed coatings using Landec's proprietary Intellicoat seed coatings through Landec Ag and other seed companies. The Corporate and Other segment includes the operations from the Company's Technology Licensing/Research and Development business and corporate operating expenses. The Food Products Technology and Agricultural Seed Technology segments include charges for corporate services allocated from the Corporate and Other segment. Corporate and Other amounts include non-core operating activities, corporate operating costs and net interest expense. Virtually all of the Company's international sales are to Asia. Operations and identifiable assets by business segment consisted of the following (in thousands):

Fiscal Year Ended May 27, 2007	Food Products Technology	Agricultural Seed Technology	Corporate and Other	TOTAL
Net sales	$ 206,180	$ 2,831	$ 1,487	$ 210,498
International sales	$ 46,406	$ ¾	$ ¾	$ 46,406
Gross profit	$ 28,252	$ 2,647	$ 1,487	$ 32,386
Net income (loss)	$ 10,916	$ 17,174	$ 1,099	$ 29,189
Identifiable assets	$ 93,985	$ 2,577	$ 44,806	$ 141,368
Depreciation and amortization	$ 2,684	$ 474	$ 102	$ 3,260
Capital expenditures	$ 6,277	$ 477	$ 28	$ 6,782
Interest income	$ 751	$ 45	$ 1,149	$ 1,945
Interest expense	$ 80	$ 171	$ ¾	$ 251
Income tax expense	$ 918	$ 1,446	$ 92	$ 2,456
Fiscal Year Ended May 28, 2006				
Net sales	$ 194,816	$ 34,096	$ 3,041	$ 231,953
International sales	$ 50,337	$ ¾	$ ¾	$ 50,337
Gross profit	$ 26,853	$ 10,439	$ 2,752	$ 40,044
Net income (loss)	$ 9,128	$ (1,387)	$ 910	$ 8,651
Identifiable assets	$ 83,531	$ 32,613	$ 2,881	$ 119,025
Depreciation and amortization	$ 2,572	$ 533	$ 98	$ 3,203
Capital expenditures	$ 4,263	$ 439	$ 44	$ 4,746
Interest income	$ 502	$ 75	$ 56	$ 633
Interest expense	$ 300	$ 152	$ ¾	$ 452
Income tax expense	$ ¾	$ ¾	$ ¾	$ ¾
Seven Months Ended May 29, 2005				
Net sales	$ 179,157	$ 25,648	$ 425	$ 205,230
International sales	$ 48,773	$ ¾	$ ¾	$ 48,773
Gross profit	$ 22,195	$ 9,448	$ 329	$ 31,972
Net income (loss)	$ 5,621	$ (316)	$ 97	$ 5,402
Identifiable assets	$ 72,511	$ 22,711	$ 4,853	$ 100,075
Depreciation and amortization	$ 2,890	$ 472	$ 105	$ 3,467
Capital expenditures	$ 3,134	$ 426	$ 98	$ 3,658
Interest income	$ 130	$ 57	$ 27	$ 214

Interest expense	$	305	$	109	$	¾	$	414
Income tax expense	$	¾	$	¾	$	¾	$	¾

16. Quarterly Consolidated Financial Information (unaudited)

The following is a summary of the unaudited quarterly results of operations for fiscal years 2007, 2006 and 2005 (in thousands, except for per share amounts):

FY 2007	1st Quarter	2nd Quarter	3rd Quarter	4th Quarter	FY 2007
Revenues	$ 51,147	$ 55,194	$ 52,956	$ 51,201	$ 210,498
Gross profit	$ 5,556	$ 8,276	$ 9,091	$ 9,463	$ 32,386
Net income	$ 14	$ 108	$ 24,644	$ 4,423	$ 29,189
Net income per basic share	$ 0.00	$ 0.00	$ 0.97	$ 0.17	$ 1.16
Net income per diluted share	$ 0.00	$ 0.00	$ 0.92	$ 0.16	$ 1.07

FY 2006	1st Quarter	2nd Quarter	3rd Quarter	4th Quarter	FY 2006
Revenues	$ 49,705	$ 53,712	$ 57,249	$ 71,287	$ 231,953
Gross profit	$ 6,590	$ 7,089	$ 11,415	$ 14,950	$ 40,044
Net (loss) income	$ (521)	$ (1,037)	$ 3,514	$ 6,695	$ 8,651
Net (loss)/income per basic share	$ (0.02)	$ (0.04)	$ 0.14	$ 0.27	$ 0.35
Net (loss)/income per diluted share	$ (0.02)	$ (0.04)	$ 0.13	$ 0.24	$ 0.32

FY 2005	1st Quarter	2nd Quarter	3rd Quarter	4th Quarter	FY 2005
Revenues	$ 46,854	$ 50,672	$ 51,532	$ 56,172	$ 205,230
Gross profit	$ 5,741	$ 5,997	$ 9,242	$ 10,992	$ 31,972
Net (loss) income	$ (692)	$ (808)	$ 2,293	$ 4,609	$ 5,402
Net (loss)/income per basic share	$ (0.03)	$ (0.03)	$ 0.10	$ 0.19	$ 0.23
Net (loss)/income per diluted share	$ (0.03)	$ (0.03)	$ 0.09	$ 0.17	$ 0.21

(b) Index of Exhibits.

Exhibit Number:	Exhibit Title
2.3	Form of Agreement and Plan of Merger and Purchase Agreement by and among the Registrant, Apio, Inc. and related companies and each of the respective shareholders dated as of November 29, 1999, incorporated herein by reference to Exhibit 2.1 to the Registrant's Current Report on Form 8-K dated December 2, 1999.
2.4	Stock Purchase Agreement between The Lubrizol Corporation and the Registrant dated as of October 24, 2002, incorporated herein by reference to Exhibit 2.1 to the Registrant's Current Report on Form 8-K dated October 24, 2002.
2.5	Purchase Agreement between the Registrant and Apio Fresh LLC and the Growers listed therein, dated as of July 3, 2003, incorporated herein by reference to Exhibit 2.1 to the Registrant's Current Report on Form 8-K dated July 3, 2003.
3.1	Amended and Restated Bylaws of Registrant, incorporated herein by reference to Exhibit 3.1 to the Registrant's Current Report on Form 8-K dated May 19, 2005.
3.2	Ninth Amended and Restated Articles of Incorporation of Registrant, incorporated herein by reference to Exhibit 3.2 to the Registrant's Registration Statement on Form S-1 (File No. 33-80723) declared effective on February 12, 1996.
3.3	Certificate of Determination of Series A Preferred Stock, incorporated herein by reference to Exhibit 3.3 to the Registrant's Annual Report on Form 10-K for the fiscal year ended October 31, 1999.
3.4	Certificate of Determination of Series B Preferred Stock, incorporated herein by reference to Exhibit 3.1 to the Registrant's Current Report on Form 8-K dated October 25, 2001.
10.1	Form of Indemnification Agreement, incorporated herein by reference to Exhibit 10.1 to the Registrant's Annual Report on Form 10-K for the fiscal year ended May 29, 2005.

Exhibit Number:	Exhibit Title
10.5*	Form of Option Agreement for 1995 Directors' Stock Option Plan, incorporated herein by reference to Exhibit 10.4 to the Registrant's Annual Report on Form 10-K for the fiscal year ended October 31, 1996.
10.6	Industrial Real Estate Lease dated March 1, 1993 between the Registrant and Wayne R. Brown & Bibbits Brown, Trustees of the Wayne R. Brown & Bibbits Brown Living Trust dated December 30, 1987, incorporated by reference to Exhibit 10.6 to the Registrant's Registration Statement on Form S-1 (File No. 33-80723) declared effective on February 12, 1996.
10.15*	1996 Landec Ag Stock Option Plan and form of Option Agreements, incorporated herein by reference to Exhibit 10.15 to the Registrant's Annual Report on Form 10-K for the fiscal year ended October 31, 1996.
10.16*	Form of Option Agreement for the 1996 Non-Executive Stock Option Plan, as amended, incorporated herein by reference to Exhibit 10.16 to the Registrant's Annual Report on Form 10-K for the fiscal year ended October 31, 1996.
10.17*	1996 Amended and Restated Stock Option Plan, incorporated herein by reference to Exhibit 10.17 to the Registrant's Quarterly Report on Form 10-Q for the fiscal quarter ended April 29, 2001.
10.18*	Form of Option Agreement for 1996 Amended and Restated Stock Option Plan, incorporated herein by reference to Exhibit 10.17 to the Registrant's Quarterly Report on Form 10-Q for the fiscal quarter ended April 30, 1997.
10.25*	Stock Option Agreement between the Registrant and Nicholas Tompkins dated as of November 29, 1999, incorporated herein by reference to Exhibit 10.25 to the Registrant's Annual Report on Form 10-K for the fiscal year ended October 31, 1999.
10.26*	1999 Apio, Inc. Stock Option Plan and form of Option Agreement, incorporated herein by reference to Exhibit 10.26 to the Registrant's Annual Report on Form 10-K for the fiscal year ended October 31, 1999.

Exhibit Number:	Exhibit Title
10.28*	2000 Apio, Inc. Stock Option Plan and form of Option Agreement, incorporated herein by reference to Exhibit 10.28 to the Registrant's Annual Report on Form 10-K filed for the fiscal year ended October 29, 2000.
10.30*	New Executive Stock Option Plan, incorporated herein by reference to Exhibit 10.30 to the Registrant's Annual Report on Form 10-K for the fiscal year ended October 29, 2000.
10.35*	1996 Non-Executive Stock Option Plan, as amended, incorporated herein by reference to Exhibit 10.35 to the Registrant's Annual Report on Form 10-K for the fiscal year ended October 28, 2001.
10.45*	Employment Agreement between the Registrant and Gary T. Steele effective as of January 1, 2006, incorporated herein by reference to Exhibit 99.1 to the Registrant's Current Report on Form 8-K dated December 15, 2005.
10.48	Supply Agreement between the Registrant and Apio Fresh LLC and the Growers listed therein, dated as of July 3, 2003, incorporated herein by reference to Exhibit 2.3 to the Registrant's Current Report on Form 8-K dated July 3, 2003.
10.53*	1995 Directors' Stock Option Plan, as amended, incorporated herein by reference to Exhibit 10.53 to the Registrant's Annual Report on Form 10-Q for the fiscal quarter ended May 25, 2003.
10.56	Form of Notice regarding acceleration of stock option vesting , incorporated herein by reference to Exhibit 10.56 to the Registrant's Annual Report on Form 10-K for the fiscal year ended May 29, 2005.
10.59	Amended and Restated Credit Agreement by and among Apio, Inc. as Borrower, and Wells Fargo Bank, National Association, dated as of November 1, 2005, incorporated herein by reference to Exhibit 10.57 to the Registrant's Quarterly Report on Form 10-Q for the fiscal quarter ended November 27, 2005.
10.63	License and research and development agreement between the Registrant and Air Products and Chemical, Inc. dated March 14, 2006, incorporated herein by reference to Exhibit 10.63 to the Registrant's Annual Report on Form 10-K for the fiscal year ended May 28, 2006.
10.64	2005 Stock Incentive Plan, incorporated herein by reference to Exhibit 99.1 to the Registrant's Current Report on Form 8-K dated October 14, 2005.
10.65	Form of Stock Grant Agreement for 2005 Stock Incentive Plan, incorporated herein by reference to Exhibit 99.2 to the Registrant's Current Report on Form 8-K dated October 14, 2005.
10.66	Form of Notice of Stock Option Grant and Stock Option Agreement for 2005 Stock Incentive Plan incorporated herein by reference to Exhibit 10.66 to the Registrant's Annual Report on Form 10-K for the fiscal year ended May 28, 2006.
10.67	Form of Stock Unit Agreement for 2005 Stock Incentive Plan incorporated herein by reference to Exhibit 10.67 to the Registrant's Annual Report on Form 10-K for the fiscal year ended May 28, 2006.
10.68	Form of Stock Appreciation Right Agreement for 2005 Stock Incentive Plan incorporated herein by reference to Exhibit 99.5 to the Registrant's Current Report on Form 8-K dated October 14, 2005.

10.70	Stock Purchase Agreement dated as of December 1, 2006 by and among the Registrant, Landec Ag and American Seeds, Inc. incorporated herein by reference to Exhibit 10.70 to the Registrant's Current Report on Form 8-k dated December 6, 2006.
10.71	License, Supply and R&D Agreement dated as of December 1, 2006 by and among the Registrant, Landec Ag and Monsanto Company incorporated herein by reference to Exhibit 10.71 to the Registrant's Current Report on Form 8-k dated December 6, 2006.
10.72*	2008 Cash Bonus Plan incorporated herein by reference to the Registrant's Current Report on Form 8-k dated May 22, 2007.
21.1	Subsidiaries of the Registrant

Subsidiary	State of Incorporation
Landec Ag, Inc.	Delaware
Apio, Inc.	Delaware

23.1+	Consent of Independent Registered Public Accounting Firm.
24.1+	Power of Attorney - See page 77
31.1+	CEO Certification pursuant to section 302 of the Sarbanes-Oxley Act of 2002
31.2+	CFO Certification pursuant to section 302 of the Sarbanes-Oxley Act of 2002
32.1+	CEO Certification pursuant to section 906 of the Sarbanes-Oxley Act of 2002
32.2+	CFO Certification pursuant to section 906 of the Sarbanes-Oxley Act of 2002

*Represents a management contract or compensatory plan or arrangement required to be filed as an exhibit to this report pursuant to item 15(b) of Form 10-K.

+ Filed herewith.

#Confidential treatment requested as to certain portions. The term "confidential treatment" and the mark "*" as used throughout the indicated Exhibit means that material has been omitted and separately filed with the SEC.

SIGNATURES

Pursuant to the requirements of section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this Report on Form 10-K to be signed on its behalf by the undersigned, thereunto duly authorized, in the City of Menlo Park, State of California, on July 27, 2007.

LANDEC CORPORATION

By: /s/ Gregory S. Skinner

Gregory S. Skinner
Vice President of Finance and Administration
and Chief Financial Officer

POWER OF ATTORNEY

KNOW ALL PERSONS BY THESE PRESENTS, that each person whose signature appears below hereby constitutes and appoints Gary T. Steele and Gregory S. Skinner, and each of them, as his attorney-in-fact, with full power of substitution, for him in any and all capacities, to sign any and all amendments to this Report on Form 10-K, and to file the same, with exhibits thereto and other documents in connection therewith, with the Securities and Exchange Commission, hereby ratifying and confirming our signatures as they may be signed by our said attorney to any and all amendments to said Report on Form 10-K.

Pursuant to the requirements of the Securities Exchange Act of 1934, this Report on Form 10-K has been signed by the following persons in the capacities and on the dates indicated:

Signature	Title	Date
/s/ Gary T. Steele Gary T. Steele	President and Chief Executive Officer and Director (Principal Executive Officer)	July 27, 2007
/s/ Gregory S. Skinner Gregory S. Skinner	Vice President of Finance and Administration and Chief Financial Officer (Principal Financial and Accounting Officer)	July 27, 2007
/s/ Nicholas Tompkins Nicholas Tompkins	Chief Executive Officer of Apio, Inc., Senior Vice President and Director	July 27, 2007
/s/ Robert Tobin Robert Tobin	Director	July 27, 2007
/s/ Duke K. Bristow, Ph.D Duke K. Bristow, Ph.D	Director	July 27, 2007
/s/ Frederick Frank Frederick Frank	Director	July 27, 2007
/s/ Stephen E. Halprin Stephen E. Halprin	Director	July 27, 2007

/s/ Richard S. Schneider, Ph.D Richard S. Schneider, Ph.D	Director	July 27, 2007
/s/ Kenneth E. Jones Kenneth E. Jones	Director	July 27, 2007

EXHIBIT INDEX

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32.1	CEO Certification pursuant to section 906 of the Sarbanes-Oxley Act of 2002.
32.2	CFO Certification pursuant to section 906 of the Sarbanes-Oxley Act of 2002.